CHAPTER-IV

TYPES OF BORROWERS AND INCOME TAX BENEFITS

A. Various Types of Borrowers

I. Individual

A person who is not infant, insane and insolvent can enter into a valid contract. When an individual is a borrower, the lender obtains a status report from independent sources. The information submitted by the borrower himself is verified in respect of accuracy. Every year, a fresh report is obtained. In case there is a glaring remarks of increase or decrease in the work of the borrower, the lender find out the reasons for such a change and review the credit limits.

i. Lunatic or Insane Person

A person seeking a contract is presumed to be of sound mind and if of unsound mind at the time of borrowing, he can avoid the contract. When a lender receives proper notice of a borrower’s insanity all operations in the account must be suspended. Now-a-days a court appoints a ‘RECEIVER’. But lender will not be safe in relying upon mere hearsay evidence of his borrower’s insanity. The lender generally ascertain the correct position before suspending operations. A contract made during lucid interval made by mentally unsound person is binding. But a certificate from two reliable medical officers regarding his mental soundness at the time of advance, has to be obtained. Banks/HFCs generally avoid lending to persons of unsound mind even temporarily.

ii. Intoxicated Person

One of the conditions of a valid contract is that it must be entered into between persons who are of sound mind. A person is said to be of sound mind for the purpose of making a contract if, at the time he makes it, he is capable of understanding it and of forming a rational judgment as to its effect upon his interests.

If a person alleges that as a result of intoxication, he was incapable of understanding the nature and terms of the contract, which fact was known to the other party, he may invoke the protection of a court of law in setting aside the contract. The onus will be

1 Indian Contract Act 1882 ; www.mortgagestrategy.co.uk/...different-types-of-borrowers/76974.a
on the party, who sets up the plea of disability to prove that it existed at the time of the contract. It should, however, be known that if a negotiable instrument has been transferred to a holder who takes it in good faith and for value, the drunken person cannot deprive the holder in due course of his rights under the instrument. It follows that the lender has to be careful in getting documents executed by persons while they are in a state of intoxication.

iii. Insolvents

When a person is unable to pay his debts and gives a notice to any of the creditor that he is about to suspend or he has suspended payment of his debts, he is said to have committed an act of insolvency. In such a case either the debtor himself or any of his creditors can file a petition in the court to declare him insolvent. The court may appoint a ‘RECEIVER’ or ‘OFFICIAL’ ASSIGNEE’ to take the possession of debtor’s property, realise the same and apportion the proceeds. When a debtor is adjudicated ‘insolvent’ he is called an ‘un-discharged Insolvent.’ However, he can again apply to the court for discharge before the specified time by the court. The court may grant or refuse such an order. If refused, he continues to be an undischarged insolvent and hence cannot enter into a valid contract. The housing finance company does not lend with or without security to an un-discharged insolvent or even to a person who is involved in insolvency proceedings.

iv. Infant or Minor

A minor is a person who has not completed the age of 18 years. In case a guardian is appointed by a court for his person or property before he has attained 18 years of age the period of minority is extended up to 21 years of age.

In terms of the Indian Contract Act, 1872 says that a minor cannot enter into a contract at all. It is not merely voidable but void ab initio. He cannot even ratify the contract made by him during minority after attaining majority.

Minor’s agreement is wholly void and not merely voidable. It follows that neither the minor nor the other party to the agreement can have it enforced in any court of law. The courts in India, however, have given a mere equitable interpretation to the dictum

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2 The Indian Contract Act 1872, section 11.
in Mohari Bhee’s case. It goes without saying that minor cannot be sued on any agreement but the question arises whether a minor can obtain the benefits of his agreement against the other party? The answer to this question is based on this dictum and principle viz. “The disability of a minor goes no further than is necessary for the protection of the minor.”

The Negotiable instruments Act, 1881 provides that a minor can draw, endorse, deliver and negotiate a promissory note, bill of exchange or cheque so as to bind all other parties except himself. A minor cannot be compelled to pay money borrowed by him even though he had misrepresented his age. A minor will have to pay only if the borrowing is done for necessities of life suited to his condition. Since the guarantee pre-supposes a debtor against whom a debt secured can be legally enforced, it follows therefore, that a guarantee given to cover an advance to the minor is worthless. Even if any security for the loan has been given by a minor, the security cannot be enforced.

The Indian Partnership Act, 1932 states that a minor may not be a partner in a firm but with the consent of all partners for the time being, he may be admitted to the benefits of partnership. But sub-section 3 further states that only minor’s share in the property of the firm or/and its profit liable for the acts of the firm. Neither the minor personally nor his other personal property can be made liable for the acts of the firm unless he repudiates his liability as a partner within six months of his attaining majority or within six month of his knowledge that he was admitted to the benefits of the partnership, whichever date is later, the erstwhile minor will thereafter be considered as a partner and will be liable in that capacity with retrospective effect from the date he was admitted to the benefits of the partnership. If a firm which includes a minor, goes bankrupt, proceedings may be taken against the firm other than minor partner or against the adult partners. Joint account with infant can be treated as Ordinary Joint Account but he cannot be made personally liable for overdraft. A minor can act as an agency. His acts will bind the principal and other parties but he is not liable.

3 Mohari Bibi v. Dharmo Das, (1903) 30 IA 114.
5 The Indian Contract Act 1872, section 68.
6 The Indian Partnership Act 1932, section 30.
v. Illiterate Person

As per customs prevailing in India, a left hand thumb impression for the gents and right hand thumb impression of the female is obtained on all documents. The latest photograph is also secured on the account opening form and specimen signature card as well. All the photographs are required to be duly authenticated by the bank. Since banker is socially bound to help such persons, requests for loans and advances are mostly considered especially under Differential Rate of Interest (DRI) Schemes i.e. the loan is granted at 4% rate of interest.

It is advisable to get the thumb impression attested by an independent witness on a separate declaration form recording that the contents of the documents were read, explained and interpreted in the language known to him or her duly signed by the witness.

vi. Blind Person

A blind person is not legally debarred from entering into a contract. But the risks in such cases arise obviously from his physical infirmity viz. his inability to see. While there is no legal provisions for appointment of a guardian of a blind person, each case has to be considered on its merits. His next of kin can be allowed to operate on the account under a proper mandate or a power of attorney. The banker has a social responsibility to advance money to a blind man who wants to earn his livelihood by opening a small repair shop, or even pan shop or when he wants to establish a small stall or even when he is appointed to man the public telephone etc. In doing so, the bank takes a calculated risk.

vii. Married Women

An Indian married woman can enter into any valid contract and can acquire, hold and even dispose of the property belonging to her absolutely. There is no distinction between a man and female (Spinster, Widow or married woman) as far as contractual capacities are concerned. She cannot bind her husband unless she acted as agent or had borrowed for necessities of life or for household. Husband can escape if he proves that there was no necessities or she was forbidden to borrow.

In case of overdraft, the banker has no remedy against her if she has no separate property or the property is settled upon her in such a way that she can use the income
only and cannot touch the corpus, nor anticipated income. In case of overdraft there is no personal remedy against a married woman as she cannot be committed to prison for non-payment of judgment debt.

In short, the banker avoid overdraft, unless, securities are offered belonging to her absolutely.

viii. Pardanashin Lady
In case of Pardanashin Lady, the burden of proof in respect of borrowing, that she fully understood the transaction and her own free will was carried out, is on the banker and hence except in exceptional cases the lender may consider small advance only if the lady is literate and of very good standing.

ix. Administrators and Executors
An executor is a person who is appointed in a ‘will’ by the testator to administer his estate according to the instructions in his will, the court has to appoint an administrator to give effect to his will.

Whereas, when a person dies intestate i.e. without leaving a will, the court may appoint an administrator to deal with the estate of the deceased and to wind up his affairs. Even if a person has left behind a ‘will’ but has not appointed executor in the will, the Court has to appoint an administrator to give effect to his will. The probate of the will or letters of administration granted by a competent court having jurisdiction over the assets or the estate or the deceased will, therefore, comprise the authority for the representatives of the deceased to deal with his estates.

x. Receivers and Liquidators
They derive their powers from the court appointing them and hence the court order is properly scrutinised by the lender to see whether they have borrowing powers. They are also made personally liable for any advance.

xi. Non-Resident and Foreign Nationals
The opening of accounts in the names of foreign nations and non-residents and operations on such accounts are subject to exchange control regulations and hence the banker should get acquainted with the relative provisions in the exchange control manual.
II. Local Authorities
The essential fact to remember while dealing with a local authority is that it is the creation of a statute which governs its borrowing powers. The banker, before making an advance to any local authority, ascertain whether it has the power to borrow under statute, the limitations on that power, the authorised form/forms of borrowing, the security which can be offered, the maximum permissible rate of interest and whether the sanction of the Government or any other appropriate authority is necessary. After looking into all these points with the help of legal advice, it would be necessary to get a resolution passed by the local body in accordance with its constitution. It follows that if the formalities attendant on the borrowings by a local authority are not complied with, the advance would become ultra vires of the local authority concerned and may consequently be irrecoverable. Since a number of legal technicalities are involved, proper legal advice would have to be taken before entertaining an advance proposal from a local authority.

III. Non-Trading Association
As provided in the Companies Act, 1956, an association (a) for promoting commerce, art, science, religion, charity or any other useful object, and (b) intending to apply its profits, or other income, in promoting its offices and prohibiting the payment of any dividend to its members, can if the Central Government gives permission in this regard, be registered with limited liability without the addition to its name of the word ‘limited’ or the words ‘private limited.’ The association on registration is subject to all the obligations of a limited company, public or private, as the case may be. In considering an advance to such an association, a banker examine its memorandum and articles of association, particularly its borrowing powers and the manner in which they can be exercised. All other precautions as in the case of limited companies should be taken. For example, a certified copy of a resolution for borrowing from the bank is obtained by the lender and the charge if so required under the Companies Act, 1956, registered. Further, lender emphasises that as these associations are not business concerns or profit-making bodies, the purpose of the

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7 The Companies Act 1956, section 25.
advance should be more carefully scrutinised. Lender also insists upon a guarantor of means, in addition to the charge on the assets of the association.

IV. Clubs & Association

Advances to clubs, associations etc., are required to be secured by the personal guarantee of all the Committee Members existing and future till the advances are liquidated. This can be arranged by taking a guarantee deed from the existing Committee members and also from new members whenever they get elected in future. In the clubs and associations may not take personal interest in liquidating the advance. Whenever a proposal is to be entertained constitution and by-laws of the club or association etc., are studied by the lender with a view to ascertaining the borrowing powers, the purpose for which an advance can be raised, the powers of the committee to charge the assets of the club or association etc., a suitably worded resolution is required to be passed by the club or association etc. and a duly certified true copy under the hand of the chairman is required to be obtained. Legal advice is also taken before considering such a loan proposal in regard to the execution of the documents and resolution etc.

V. Trust Accounts

Trustees have no individual powers. They all have to act together and cannot delegate their authority to any other person even to one among themselves unless provided in the trust deed. They do not have any implied powers to obtain advances against trust properly, unless specifically authorized to do so by the trust deed. Without any express powers in this regard, they cannot pledge/mortgage/charge the trust property. An advance in a trust account is made after getting the trust deed properly examined by lender’s legal adviser. In case such an advance is permissible, proper documents should be drawn up in consultation with the legal adviser. The advance is considered only when the trustees are highly respectable men of good means. Personal guarantee of trustees is obtained. A charge on trust property, if the trust deed so permits, should be obtained.

VI. Joint Account Holders

The Indian Contract Act, 1872 provides; ⁸

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⁸ The Indian Contract Act 1872, sections.42,43,44,45.
When a person has made a promise to two or more persons jointly, then unless a contrary intention appears from the contract, the right to claim performance rests, as between him and them, with them during their joint lives and after the death of them, with the representatives of such deceased person jointly with survivors and after the death of the last survivor, with the representatives of all jointly. It is, therefore, provided:

1. Joining of all promisees in giving a valid and effective discharge.
2. And the devolution of joint rights upon the legal representatives of the deceased promises.

Regarding borrowing in joint accounts the following 3 sections can be refereed:

**Section 42:** When two or more persons have made a joint promise, then unless a contrary intention appears from the contract, all such persons during their joint lives, and after the death of any of them, his representatives jointly with the survivors, and after the death of the last survivor the representatives of all jointly must fulfil the promise.

**Section 43:** When two or more persons make a joint promise the promise may, in the absence of express agreement to the contrary compel any one or more of such promisors to perform the whole promise.

**Section 44:** Where two or more persons have made a joint promise, a release of one of such joint promisors by the promisee, doe not discharge the other joint promisors.

It is, therefore, necessary that when a banker/lender opens a joint account, clear instructions should be obtained in writing as to how and by whom the account will be operated or whether any body of them is authorised to operate the account.

**Joint and Several Liability**

Separate liabilities are established in case of Joint liability. The banker has only one action, whereas in the case of several liability he has as many rights of actions as there are debtors. In case of joint liability only if one of the joint debtors dies, the creditor can claim against the estate of the deceased joint debtor only to the extent of the debt due at the time of his death with the survivors.

The financers generally remember the following points in case of joint accounts:
1. All the joint parties should invariably joint in the application for any advance and in signing all the relevant documents.

2. If shares and or other securities are standing in joint names, the relative transfer deeds must be signed by and or endorsements on securities made by all the parties to the same.

3. An undertaking signed by all the joint account holders to the following effect, has be taken.
   a. That none of them is a minor.
   b. That they shall give a proper notice to the bank in case of death, insolvency or insanity of any one of them.
   c. That any one of them or any one of the survivors or the last survivor shall have the full authority to acknowledge debts an securities on behalf of all of them.
   d. That any one of them or any of the survivors of them or the last survivor as the case may be, shall have the authority not only to lodge and charge the securities with the bank but also withdraw the same from the bank. In the absence of such instructions, the account should be operated upon only jointly by all and papers and documents should also be signed by all of them.

Death, Insanity or Insolvency of any Joint Account Holder

Death, insolvency or insanity of a joint account holder puts an end to the mandate (Authority given or instruction given) and operations on the account will cease.

Death: When a joint holder dies, it is necessary to stop operations in the account or break the account so as to preclude the operation of the rule in Clayton’s case\(^9\).

Although the estate of the deceased is not freed from liability to pay the debt due at the time of death, breaking of the account will ensure that such liability is not reduced by subsequent payments.

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\(^9\) An 1816 English case which established a presumption that monies withdrawn from money account are presumed to be debts from those monies first deposited. *Devaynes v. Noble* (aka clayton’s case) 1 Mer.572 als 35 E.R. 781 (1816)
**Insolvency:** The same procedure as in the above case will apply. However, if the borrowers are jointly and severally liable (the banker invariably ensures this), the lender can prove for the entire debt, ignoring the solvent account holders and treating any securities deposited by them as collateral. Any security charged by the insolvent customer must be sold or valued and the claim filed only for the balance.

**Insanity:** The lender besides following the above procedure promptly should review the whole position including the worth of such borrower, and decide about continuation of the facility/reduction of the facility/adjustment of the entire account. If at all the guarantee agreement becomes necessary while obtaining fresh set of documents from the surviving joint account holders if the banker decides to continue the advance.

**VII. Joint Hindu Family or Hindu Undivided Family (H.U.F.)**

The above system is very peculiar to Hindus. A Hindu Undivided Family (H.U.F.) consists of all the descendents in the male line from a common ancestor, their wives and daughters. This system has acquired a special position in trade and commerce in India.

There are two schools of Hindu law:

1. **Mitakshara Law**, which is prevalent throughout India except Bengal, believes that all male members acquire a right in the co-parcenary by birth. One common living ancestor and his male descendents up to three generations next to him constitute , “co-parcenary”. After the 2005 amendments to the Hindu Succession Act, 1956, even the daughters of the male coparceners are made coparceners just like their male counterparts.10

   A male co-parcener acquires the right to H.U.F. property not only after his birth but even from the time of his conception. A banker, therefore, must exercise special caution because there is a danger of the transaction, impugned by a person who was not even born at the date of transaction.

2. **Dayabhaga School**, which prevails in Bengal, denies the doctrine of right over property by birth. According to them, father is the absolute owner of the property and practically given him unrestricted powers over it. It may be remembered that

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10 Hindu Succession Act 1956, Section 6 as amended by Hindu Succession (Amendment) Act, 2005.
there is no bar of owning a separate self-acquired property by a Hindu co-parcener besides having a share in H.U.F. property. Karta, i.e. either the father or some other senior most male member manages the property of HUF. Though Karta is a Manager of H.U.F. it is likely that another person may be appointed as Manager in a trading HUF business. Karta is entitled to be in physical possession of HUF property and has a right to manage the same. He is not the agent of the co-parceners since he is not a partner as in the partnership firm. He has power to borrow, alienate the joint property or even incur any obligation so as to bind the whole of the property without the consent of other co-parceners, only if the borrowing is done for a legal necessity or for benefit of estate. Some examples are:

1. Maintenance and education of family.
2. Marriage or thread ceremony of co-parcener.
3. Performance of funeral ceremonies or other rites.
4. Cost of litigation necessary to preserve the estate.
5. Costs or payment of debts incurred for family business.

The banker/hfc take following precautions while advancing the money to the H.U.F. Obtain H.U.F. declaration form and keep the same with loan. Documents. Karta should be asked to submit a complete List of co-parceners giving the dates of birth of minor co-parceners.

When a minor co-parcener attains majority, his signature should be obtained signifying his assent by way of notification of the undertakings already given by co-parceners. Obtain a letter of undertaking signed by all co-parceners,
(a) That the credit facilities are necessary and beneficial to the family estate and will be utilized for the benefits of the family.
(b) That Shri_____. Karta of the Hindu Undivided family, is authorised to charge, lodge and withdraw any security of the Hindu Undivided Family on our behalf and that all the dealings and transactions entered into by the Karta with your Bank, shall be binding on us.
(c) That Shri_____. Karta of the Hindu Undivided family is authorized to acknowledge the debts of the Hindu Undivided family by signing documents in your favor from time to time.
(d) That in the event of death or lunacy or insolvency of Karta, we shall give you a written notice on this effect and we shall continue to remain liable to the Bank until all our dues are paid off.

(e) That Shri ____________, Karta of the Hindu Undivided Family is also authorized to approach the Bank for raising loan and sign and execute the necessary loan documents in favor of the Bank on behalf of the Hindu Undivided Family.

Finally, we undertake that the above undertaking shall remain irrevocable until all our accounts are cleared and closed.

Yours faithfully,

(1)…………………………………………..
(2)…………………………………………..

Co-parceners of…………..(H.U.F.)

This letter should be signed by all the co-parceners of the Hindu Undivided Family. In case of minor co-parceners, their guardians should sign on behalf of such minors.

Facilities excepting against Fixed Deposit Receipts, Life Insurance Policies, Govt. Securities such as National Saving Certificates, Post Office Time Deposit certificates (d) Jewellery etc., should be guaranteed by Karta and all other major co-parceners in their personal capacity. The banker has to ensure that any facility granted to HUF are utilised for the exclusive benefit of the family business only and there should not be any diversion of funds because the burden of proof is on the bankers upon the filing of a suit. Stop all operations in the account the moment the bank receives a notice of death, lunacy or insolvency of Karta. It is necessary to review the whole position of the accounts and take further steps to continue, reduce or adjust the facilities. If at all, the guarantees were obtained from Karta and or adult co-parceners, or even outsiders, a fresh deed of guarantee will be necessary if any of the eventualities occur. Karta can acknowledge debts binding on the joint family, as to extend the period of limitation.

**Liabilities of Co-parceners:** It is generally presumed that money required for carrying on the family business is a legal necessity and that the business is carried on with the consent and for the benefit of the members of the family. It follows, therefore, that if debts are incurred by the Karta or Manager in the ordinary course of the family business, the co-parceners become liable. Their liability, however, is not
beyond their share in the co-parcenary that. Lenders/Banks, therefore, in order to make adult co-parceners personally liable, require them to be the contracting parties alongwith the Karta. In other words the Karta and all the adult co-parceners must sign all the necessary documents in their personal capacities also.

**Partnership Firms**

**Definition:** Partnership is defined in the Indian Partnership Act, 1932 as ‘the relation between persons who have agreed to share the profit of the business carried on by all or any of them acting for all.” No partnership can consist of more than 20 persons. In the case of a firm carrying on Banking business, the maximum permissible number is 10 persons.

**Computation of number**

1. If a firm includes one or more partnership firms, the partners of all such firms and the partners of the original firm, are being added individually as members of the partnership. It may be mentioned here that a partnership firm cannot become a partner of another firm because it is not a legal person. However, the partners may be partners in another firm in their individual capacity lost sight of when proposals for advances to partnership firms are considered.

2. When a partnership includes a limited company, the company is to be treated as one member only.

3. When a partnership includes H.U.F. the number of adult co-parceners of family will be individually added up to ascertain the strength of partnership. H.U.F. is also not a legal entity and hence it should not become partner in a partnership firm. However, the Karta of a H.U.F. or any of its co-parceners can become a partner in his individual capacity. A Karta can enter into partnership with other individuals. In such a case the words representing an individual as well as the Karta would be as follows:

   “P.Q.R. and X as Karta of his H.U.F.;
   M/s. XX. And Sons”

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11 Indian Partnership Act 1932.
Registration of a firm

The Indian Partnership Act, 1932\(^\text{12}\) requires that every firm should be registered with the Registrar of Firms of the state in which it has its Head Office. Consequences of non-registration are:

1. An unregistered firm cannot bring any suit to enforce a right arising out of contract against an outsider. But it can bring a suit to enforce a right arising otherwise than out of a contract.
2. A suit filed by an unregistered firm is not maintainable and even its subsequent registration does not save it.
3. The right of a third party to proceed legally against a firm or its partners is not affected only because the firm is not registered. However, it is preferable for the bankers to sanction credit facilities to registered partnership firms and the relevant partnership deed obtained. It is also a practice among the bankers to obtain a ‘partnership Declaration Form’ signed by all the partners in their individual capacity. The partnership deed should be duly scrutinized and closely studied to find out if any restrictions have been imposed on one or more partners to open, operate or overdraw the account and any limitations are imposed on borrowing powers. It may be noted that if both partnership declaration form and partnership deed are obtained by the banker, the deed will prevail and declaration form will be treated as cancelled.

Section 19 of the Indian Partnership Act, 1932 states that every partner is an agent of his firm and his other partners for the purpose of the normal business of the firm. It, therefore, follows that each partner has implied authority to bind the firm and other partners. This implied authority of the partners is subject to the provision that the firm can only be bound by what is done or executed in the firm’s name or in another manner expressing or implying an intention to bind the firm by such acts of the partner as are necessary in the usual course of the firm’s business.

To outside world a partner is an unlimited agent of the firm and other partners as stated earlier, but only in the matter connected with the normal business of partnership in respect of private arrangement. Notice to any partner of any matter relating to partnership affairs operates as notice to the firm except in case of fraud on the firm.

\(^{12}\) The Indian Partnership Act 1932, section.58.
committed by or with consent of that partner. However, in absence of any usage or custom, the implied authority does not empower the partners to:

1. Submit a dispute relating to business to arbitration.
2. Open a bank account in his name on firm’s behalf.
3. Compromise or relinquish any claim by firm.
4. Withdraw a suit filed on behalf of firm.
5. Admit any liability in a suit against the firm.
6. Acquire immovable property on behalf of the firm.
7. Transfer immovable property belonging to the firm.
8. Enter into partnership on behalf of the firm.

**Minor as a Partner**

A minor can be admitted to the benefits of a partnership with the consent of all the partners for the time being. The share of a minor in a firm (including his share in profit) is liable for the acts of the firm but not his person or his other personal property. A minor may repudiate his liability as a partner within six months of his attaining majority or within six months of his knowledge that he was admitted to the benefits of partnership, whichever date is later. His silence after the expiry of the above period will be taken to mean, in law, that he has elected to be a partner. He will thereafter be liable in that capacity with retrospective effects from the date he was admitted to the benefits of the partnership. An agreement of partnership wherein a minor has equal rights with others in regard to profits and equal liability for losses is void and unenforceable.\(^\text{13}\) It should be emphasized that a minor is incompetent to contract. His guardian cannot, therefore, enter into an agreement of partnership with third party on behalf of his ward and make the minor personally liable as a partner.

**Limited Company as Partner**

Whenever a limited company is a partner in a partnership firm all the precautions relevant in the case of limited companies should be kept in view and relevant instructions complied with. Further in case a limited company is a partner, the whole of the liability of the firm can be recovered from the company alone, subject of course to the extent of its assets. No shareholder of the company would be personally liable.

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\(^{13}\) *Dharam Vir v. Jagan Nath and others*, AIR. 1968 Panjab 841.
for the company’s liability, unless he has guaranteed the facility in his personal capacity.

A question may arise whether a charge created by a firm in which a limited company is a partner, requires registration, under the Companies Act, 1956.\textsuperscript{14} The point is not free from doubt. The safer course however, appears to be to have such a charge (if covered under Section 125 of the Act) registered with Registrar as if the company is itself a borrower. Necessary documents for registration of charge are obtained for the purpose.

**Mortgage of Immovable Property**

Implied authority of a partner does not extend to the transfer of immovable property belonging to the firm; he has no authority to bind his co-partners by a mortgage deed executed by him alone. All partners must sign or authorize any one of them to execute the mortgage deed.

**Guarantee**

A partner has no implied authority to sign and guarantee on behalf of the firm. All partners must sign the guarantee form. However, if giving of guarantee is the normal business of the firm, one partner can bind the firm and other partners.

**Change in the Firm’s Constitution**

**Admission of a New Partner**

If at the time of admission of a new partner, the firm’s account is overdrawn, the incoming partner will not be liable for the balance due at the date of his admission into the firm, unless he expressly contracts with the firm and also with the firm’s creditor (bank/hfc) to accept liability in that connection.

**Retirement of a Partner**

Retiring partner must give a notice to the Bank. If he does not serve such notice, he will continue to be liable for all advances made to the firm even after his retirement till the date of notice. In practice, the banker releases the retiring partner and accepts the newly constituted firm as its debtors. In case the banker does not want to oblige,
he break the account and stop operations to avoid application of the rule in Clayton’s case.\(^{15}\)

**Death of a Partner**

The legal effect is dissolution unless provided contrary in the deed. Surviving partners can continue to operate in the account for winding up purpose. Cheques signed by deceased partner requires confirmation from all surviving partners before they are paid. It is advisable to break the account as in the case of retirement of a partner to preserve the rights against the estate of the deceased partner.

**Insolvency of a Partner**

Insolvency of all the partners or all the partners except one automatically dissolves the firm unless otherwise provided. Cheques signed by insolvent partners is not to be honored without obtaining confirmation of other solvent partners. The banker /lender follows the same procedure of breaking the account as indicated earlier.

**Insanity of Partner**

If one of the partners becomes of unsound mind, a suit for dissolution of the firm can be filed by the next friend or by any other partner. The procedure to be adopted is virtually the same as that which is to be observed on the death or insolvency of a partner.

**IX. Companies**

A company is an association of persons, incorporated to promote, by joint contribution to a common stock or capital, the carrying on of some enterprise, usually commercial.

**a. Types of Companies**

**(i) Companies Limited by Shares**

The liability of share-holder is limited to the amount of share capital, if any remaining unpaid on the shares held by him.

**(ii) Companies Limited by Guarantee**

Each member undertakes to be liable to contribute to the assets of the company up to a certain amount (which he has undertaken) in the event of its liquidation.

\(^{15}\) Claytons case 28 (1816) 1 Mer 572 p608 (Banking Kaw).
(iii) Unlimited Companies

The very name implies that the liability of members is unlimited. But such companies are very rare.

Under each of the three heads mentioned above, there may be ‘private’ as well as ‘public’ companies.

iv. a. Private Company:

1. Restricts the right to transfer the shares.
2. Limits the maximum numbers of members to 50, excluding present or past employees who may also be members (minimum only).
3. Prohibits any invitation to the public to subscribe to its shares and debentures.

b. Public Company: It is one which is not private company. It must have minimum 7 members. There is no maximum limit of number of members.

c. The Registered Office: All notices and documents must be served on the registered office of a limited company. A document to be properly served upon a company or an officer thereof must be sent to the company or the officer at the registered office of the company by post under certificate of posting or by registered post or by leaving it at the registered office. Statements of account and general routine correspondence relating to day-to-day business matters may be sent to other offices of the company as required but legal notices must be served on the registered office. While entertaining any proposal for advance to limited company the lender has to call for following documents:

1. Memorandum of Association

It is a constitution of the company and prescribes the area beyond which the actions and activities of the company cannot go. It lays down the objects of the company and purpose for which it is formed. Any act, outside the permitted range is said to be “Ultra Vires” the company and hence Void. Such acts cannot be validated even by unanimous assent of the members at General Body Meeting. A certified true copy of this document should be obtained.

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16 The Companies Act 1956 section 252.
17 Ibid. section 51.
18 Indian Companies Act,1956.
2. **Articles of Association**

It deals with the internal regulations of the company and lay down the manner in which the business is to be conducted. A public limited company with share capital need not register its separate articles of associations but may adopt instead a bunch which contains a model set of articles. Even where a company files its own articles, regulations shall apply to it if it has not specifically excluded or modified any or all regulations. The articles, being subsidiary to the memorandum, cannot empower, the directors to do anything which is beyond the power of the company as set out in the memorandum. Certified true copy of articles of association must is being obtained by the lender.

3. **Certificate of Incorporation**

The Registrar of Companies issues this certificate after being satisfied that all requirements of the Companies Act in respect of registration have been complied with. The company comes into existence as a separate legal entity from the date of incorporation and hence it is also known as Birth-certificate (The original should be inspected and returned by the bank and a certified true copy thereof be obtained and kept on record recording wherein a note to the effect that original seen’).

4. **Certificate to Commence Business**

In the case of public limited company this certificate is a must. No public company can commence business or exercise borrowing powers unless this certificate is issued to it. This certificate is not required by private limited company. However, public limited financial companies are required to obtain certificate of registration from Reserve Bank of India and housing finance company from the National Housing Bank prior commencing the business. Here it is specifically mentioned that provisions of the National Housing Bank act, 1987\(^\text{19}\) overrides similar provisions of other Acts. These financial companies (NBFCs and HFcs), therefore, can obtain a certificate of commencement of business from the registrar of Companies once registration certificate is obtained from the Reserve Bank of India/National Housing Bank as the case may be.

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\(^{19}\) Chapter V, Indian Companies Act, 1961.
5. Borrowing Powers

Under the Companies Act, 1956\textsuperscript{20} no public limited company or private company which is subsidiary of a public limited company can borrow sum or sums of money which put together may be more than its own paid-up capital plus free reserves, if any except with the consent and authority of the shareholders obtained in a general meeting by way of a resolution. This general body meeting resolution should also be certified by the Chairman of the meeting that the same has been duly entered in the Minute Book and signed therein by the Chairman of the Meeting.

For every credit facility there should be specific resolution of the Board of Directors empowering one or more of their Directors Officials to raise the loan and charge the security to execute documents, to operate upon such accounts, and to confirm the balances from time to time. This Resolution should specifically mention the amount of credit facility. The Resolution must be passed in a meeting of the Board of Directors and not by circulation, as a Resolution passed by circulation is of no value for raising a loan.\textsuperscript{21}

6. Restriction on the borrowings by the company

The Memorandum of Association of the limited company should be scrutinised to ascertain that the purpose and the amount of accommodation sought are authorized by the Memorandum of Association. It must be ascertained whether there is any restriction of the borrowing by the company. If a restriction is found in the Memorandum of Association and the company borrows in excess of this restriction, such borrowing would be \textit{ultra virus} of the company and cannot be regulated even by the general meeting. The Bank then cannot avail itself of any of the company’s security held to cover such borrowing.

It should also be ascertained from Memorandum of Association and Articles of Association, that the directors are empowered to borrow and create charge on the assets of the company whether movable or immovable. Care should also be taken to see that all the provisions of the Indian Companies Act, 1956 and amendments thereof have been complied with.

\textsuperscript{20} The Companies Act 1956, section 293 (1) (d).
\textsuperscript{21} The Companies Act 1956 section 272.
7. Common Seal
At the time of execution of loan documents the lender must carefully read the provisions of the Articles of Association of the company which relate to the Common Seal of the Company and note to comply with the same.
In case the resolution empowering any Director (s)/official to execute loan documents is also mentioned the affixation of common seal on the loan documents, resolution must be very clear with regard to the mode of such affixation and the personnel(s) in whose presence it is to be affixed. Reference should also be made to the provisions of Articles of Association to ensure if the resolution and the execution of documents are in consonance with the provisions as laid down in the Articles of Association.

8. Execution of Loan Documents
The lending institution should ensure that the documents are executed by the Directors officials duly authorized by the relevant Board Resolution.

9. Limited Companies as Guarantors
Since under the Companies Act, there are some restrictions on guarantees by limited companies, the bank should refer all such cases to their legal advisers before accepting such guarantees.\(^{22}\)

10. Guarantee of Directors
It is necessary that all the facilities granted to private limited companies are guaranteed by the Directors of the company in their personal capacities. In case of advances to public limited companies, personal guarantee of guarantors should be stipulated wherever suggested by the circumstances.

11. Charge
Branches should conduct a search in the office of the Registrar of Companies before allowing any advance to companies whether private or public wherever his charge requires registration with Registrar of Companies. Where, a charge on the assets of the company is required to be registered under the Indian Companies Act, branches should get the charge registered immediately after its creation and without relying on the prescribed period of 30 days.\(^{23}\)

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\(^{22}\) Section 11

\(^{23}\) Section 11.
12. Negative Lien

If the borrowing company states that its assets are unencumbered and free of any charge, they should be asked to pass a resolution in the following form:

The company hereby declares that all its fixed and current assets are free from any charge or encumbrances and that all the fixed and current assets either existing or which may be acquired in future will not be sold of, charged, mortgaged, hypothecated, delivered or disposed of in any other manner so long as the company remains indebted to the bank.

The above wordings may be amended to suit individual cases. The above resolution should preferably form a part of the resolution by the company to take the proposed facilities from the Bank.

B. Tax Benefits

i. Income Tax Benefits on EMI

Very often tax payers take loans either for the purpose of buying a house or a flat. They are required to pay equated monthly instalments (EMI) of interest and principal. In some cases both the interest and principal are deductible for purposes of income tax and in some cases it is not so deductible. The benefits of EMI under the Income Tax Act in relation to home loans are discussed herein.

House should be ready for occupation

One of the most important aspects to be remembered by a tax payer is that the house or flat must be complete. If the house is not ready or is still under construction, then no deduction either on principal or interest would be allowable and permissible under the Income Tax Act.

Bifurcate EMI into Interest and Loan

The next important aspect to be remembered by a tax payer is to bifurcate EMI into two parts. They are (i) Interest and (ii) Principal. This is because the deduction of interest as well as principal is governed by different sections of Income Tax Act. Therefore, this is the most important aspect to be remembered by a tax payer.

**Full interest deductible on let out house**

If the house is let out by the taxpayer, then the entire interest irrespective of the amount is fully deductible under Section 24 of the against income from House Property. In case the interest amount is more than the net rent, the loss under the heading “Income from House Property” can be adjusted against other income. It can even be carried forward in the future years.

**EMI instalment for acquisition also deductible**

Under the provisions of the Income Tax Act, 1956\(^{25}\) the amount of EMI pertaining to the payment of principal for acquiring the house is allowable within the overall limit of Rs. 1,00,000. This is for the purpose of acquiring a house through Delhi Development Authority or other housing boards like Haryana Urban Development Authority (HUDA) or any other housing authority. The overall limit in this case is Rs. 1,00,000.

**Repayment of loan deductible**

Under the provisions of Section 80C (2) (xviii) deduction up to Rs. 1,00,000 in respect of repayment of loan is permissible. The repayment of the amount borrowed for home loan by the assessee is deductible only if it is from Central Government or any State Government, or any bank, including co-operative bank, or the Life Insurance Corporation (LIC), or the National Housing Bank (NHB), or a Public Sector Company providing housing finance, or any co-operative society providing housing finance or where the employer is an authority or a Board or a Corporation or any other statutory body or the employer is a Public Company or public sector company or a university or an affiliated Central Government or a local authority or a co-operative society. Besides, stamp duty, registration fee and other expenses for the purpose of transfer of such housing property to the assessee is also deductible under Section 80C.

Tax benefits that come with home loans are a major reason why many people eagerly join the bandwagon of homeowners. The principal repayment that borrowers make on their home loans is eligible for income tax deduction under Section 80C of the Income Tax Act, 1956. The limit under Section 80C is Rs. 1 lakh in case of self occupied property.

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\(^{25}\) The Income Tax Act 1961, section 80C (2).
Self-Occupied Property
Suresh’s taxable income is Rs.9 lakhs. The principal component of the EMI that he repays to the lender annually comes to around Rs.79,638. Suresh can deduct the home loan principal amount repaid from his taxable income directly. Therefore, his taxable income becomes Rs. 9 lakhs minus Rs. 79,638 - i.e. Rs. 8.20 lakhs. He can invest in other instruments mentioned under Section 80C and further reduce his taxable income by another Rs. 20,000.

Home owners can avail tax benefits on the interest component repaid under the income tax Act\textsuperscript{26}. The maximum amount of interest that can be deducted from your taxable income for a self-occupied property is Rs. 1.5 lakhs. As a result, taxable income decreases by that amount. Suppose Suresh has repaid Rs.1.9 lakhs towards the interest component of the existing home loan in one assessment year. Since there is a limit of Rs. 1.5 lakhs, he can deduct this amount from his income.

Property investors can get tax benefits on a second residential property also.\textsuperscript{27} Suresh purchased a two bedroom apartment for Rs 18 lakhs five years ago. He intends to purchase another apartment for Rs 20 lakhs. His monthly gross taxable income is roughly around Rs 75,000. He decides to rent out his second house.

What are the tax sops he is entitled to?
Suresh has found a lender who is willing to give him the huge loan amount. The loan amount for his first house is Rs. 18 lakhs. For a loan tenure of 15 years and interest rate of 13 percent, his monthly EMI outflow comes to Rs 22,774 approximately. The loan amount for his second house is Rs 20 lakhs. For loan tenure of 20 years and interest rate of 13 percent, his monthly EMI outflow comes to Rs 23,430 approximately.

The EMI calculated by the lender depends upon the loan amount, interest rate charged for the loan and loan tenure. EMI is an uneven combination of the principal and interest components. During the initial years, lenders collect more interest than principal but as the tenure approaches the end, the principal component of the loan increases. In the beginning, a major portion of the EMI as high as 90 percent goes in servicing the debt.

\textsuperscript{26} The Income Tax Act 1961, section 24.
\textsuperscript{27} Times Property Legal issues, 2008.
How tax benefits work for Suresh

<table>
<thead>
<tr>
<th>House category</th>
<th>Annual Interest</th>
<th>Annual principal</th>
<th>EMI</th>
</tr>
</thead>
<tbody>
<tr>
<td>Self occupied prop.</td>
<td>1,93,655</td>
<td>79,638</td>
<td>22,774</td>
</tr>
<tr>
<td>Rented Property</td>
<td>2,58,691</td>
<td>22,487</td>
<td>23,432</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Tax head</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross taxable income (from salaries, interest etc)</td>
<td>9,00,000</td>
</tr>
<tr>
<td>Principal deduction on self-occupied prop. - Section 80C.</td>
<td>79,638</td>
</tr>
<tr>
<td>Interest deduction on self-occupied prop. - Section 24</td>
<td>1,50,000</td>
</tr>
<tr>
<td>Rental income (full) at Rs 8000 per month - (not included in calculation - shown for information only)</td>
<td>96,000</td>
</tr>
<tr>
<td>Rental income (adjusted) at 70 percent of full rented income</td>
<td>67,200</td>
</tr>
<tr>
<td>Interest deducted on property rented out</td>
<td>2,58,691</td>
</tr>
<tr>
<td>Net taxable income</td>
<td>5,74,871</td>
</tr>
</tbody>
</table>

**Second Property**

For Suresh second house, there are no benefits of principal deduction like in the self-occupied property. Homeowners can, however, claim benefits for interest repayment of home loan.28 The rental income earned by the second property has to be shown taxable salary with up to 30 percent deduction on rental income allowed as deduction towards property tax and maintenance.

**ii. Tax Benefits on Home Loans**29

In the last few years, if property has turned out to be one of the attractive investment options, the credit should also go to banks and housing finance companies which were generous in their home loan policy. The bank’s/housing finance companies willingness to lend was largely driven by the tax sops enjoyed by borrowers on their home loans. If one is wondering what the tax sops offered on home loans are, here is a quick ready beckoner.

**How beneficial are home loans?**

In recent times, a home loan has proved to be one of the biggest tax relief providers thanks to the tax sops offered on them. Under Section 24 of the Income Tax Act, the interest paid on the home loan qualifies for tax deduction up to a maximum limit of

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Rs. 1.5 lakhs. This is irrespective of the income category of the borrower which means it is available to all categories of assesses.

In addition, the borrower can also claim a tax benefit, up to a limit of Rs. 1 lakh towards the principal repayment. When a loan is repaid through EMIs by the borrower, a portion goes towards the interest and the balance goes towards principal repayment. In the early part of the loan period, the interest component tends to be higher while the principal component will be negligible. The principal repayment, however, is covered under Section 80C which means a borrower can plan his tax after taking into account this amount.

If we take into account both interest and principal components, one can enjoy a tax relief of Rs. 76,500 on Rs. 2.5 lakh loan.

**Income tax slab for fy 2012-13**

The Income Tax Slab for fy 2012-13 / ay 2013-14 are slightly different from Income tax slab for fy 11-12. As per the union budget presented by Finance Minister Pranab Mukherjee on 16th March 2012 the newly proposed income tax rates the slab ranges have been revised upwards but the changes are not much significant in the 10% tax bracket.

In income Tax Slab for ay 13-14 / fy 12-13, basic tax exemption limits are revised and the Indian finance ministry has also broadened the tax slabs for men and senior citizens. The threshold income tax exemption limit for men has been revised to Rs 2,00,000 than the previous limit of Rs 1,80,000. There will be a minimum saving of Rs 2000 in income tax than previous year. The 20% slab has been widened and its limit has been raised from 8 lakhs to 10 lakhs. So there will be an additional saving of Rs 22000 in tax if your taxable income is Rs 10,00,000 as compared to previous year. 30% tax slab will now start from Rs 10,00,001. The budget also exempt up to Rs 10,000 of interest income from tax. There is no change in tax structure for women and senior citizens. In new tax structure tax exemption of Rs. 20,000 on investment in tax saving Infrastructure bonds is also maintained and there is no change in this as compared to previous year. This is in addition to exemption of up to Rs. 1, 00,000 already allowed under specific savings instruments. The new and revised income tax slabs and rates applicable for the financial year (FY) 2012-13 and assessment year (AY) 2013-14 are mentioned below:
New Income tax slab for fy 2012-13 / ay 2013-14

New Income Tax Slabs for ay 13-14 for Resident Senior Citizens above 60 years (FY 2012-13)

<table>
<thead>
<tr>
<th>S. No.</th>
<th>Income Range</th>
<th>Tax percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Up to Rs 2,50,000</td>
<td>No tax / exempt</td>
</tr>
<tr>
<td>2</td>
<td>2,50,001 to 5,00,000</td>
<td>10%</td>
</tr>
<tr>
<td>3</td>
<td>5,00,001 to 10,00,000</td>
<td>20%</td>
</tr>
<tr>
<td>4</td>
<td>Above 10,00,000</td>
<td>30%</td>
</tr>
</tbody>
</table>

New Income Tax Slabs for ay 13-14 for Resident Senior Citizens above 80 years (FY 2012-13)

<table>
<thead>
<tr>
<th>S. No.</th>
<th>Income Range</th>
<th>Tax percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Up to Rs 5,00,000</td>
<td>No tax / exempt</td>
</tr>
<tr>
<td>2</td>
<td>5,00,001 to 10,00,000</td>
<td>20%</td>
</tr>
<tr>
<td>3</td>
<td>Above 10,00,000</td>
<td>30%</td>
</tr>
</tbody>
</table>

New Income Tax Slabs for ay 13-14 for Resident Women (below 60 years) (FY 2012-13)

<table>
<thead>
<tr>
<th>S. No.</th>
<th>Income Range</th>
<th>Tax percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Up to Rs 2,00,000</td>
<td>No tax / exempt</td>
</tr>
<tr>
<td>2</td>
<td>2,00,001 to 5,00,000</td>
<td>10%</td>
</tr>
<tr>
<td>3</td>
<td>5,00,001 to 10,00,000</td>
<td>20%</td>
</tr>
<tr>
<td>4</td>
<td>Above 10,00,000</td>
<td>30%</td>
</tr>
</tbody>
</table>

New Income Tax Slabs for ay 13-14 for Others & Men (FY 2012-13)

<table>
<thead>
<tr>
<th>S. No.</th>
<th>Income Range</th>
<th>Tax percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Up to Rs 2,00,000</td>
<td>No tax / exempt</td>
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<td>2,00,001 to 5,00,000</td>
<td>10%</td>
</tr>
<tr>
<td>3</td>
<td>5,00,001 to 10,00,000</td>
<td>20%</td>
</tr>
<tr>
<td>4</td>
<td>Above 10,00,000</td>
<td>30%</td>
</tr>
</tbody>
</table>

For normal category the simple calculation is as follows

- Taxable Income in 10% slab maximum tax will be Rs 30000
- Taxable Income in 20% slab maximum tax will be Rs 30000 + Rs 1,00,000 total Rs 1,30,000
- Taxable Income in 30% slab minimum tax will be Rs Rs 1,30,000

Education and other cess will be in addition to this.
Co-applicants and tax benefit
A common question among borrowers is whether more than one borrower can take advantage of the home loan benefit. For claiming a tax benefit jointly, the primary requisite is that the borrowers should prove that the loan is serviced jointly even if the property is in one individual’s name. For instance, a husband and wife can jointly claim tax benefits on their home loan if they are servicing the loan jointly. The joint tax benefit need not be in equal terms and can vary according to the contribution.
Is it restricted to only one property?
The tax benefit on a home loan is provided to the first property. However, one can borrow for more than one property and in the case of second property, there would be a deemed income from the second property even if it is not let-out. For the purposes of tax benefit, the interest component of both loans can be considered.
Some conditions for tax benefits
Benefit for built property:
Banks and housing finance companies may be willing to give loans for the purchase of land but a borrower cannot enjoy tax benefits on such loans. As a result, even if your loan for the purchase of land is considered a home loan by the banker, it does not entail you any tax benefit. Hence, from an income tax point of view, it may be prudent to go in for a composite loan which allows the borrower to opt for construction loan too.
Benefit on occupancy: As per the Income Tax Act, the tax benefit on a home loan is provided to a self-occupied property. This means a borrower cannot claim tax benefits unless he is in possession of the property. Till such time, the interest paid on the home loan would be considered pre-EMI interest without any tax benefits.
iii. Tax Deduction on House Rent Allowance (HRA)30
A person can claim exemption on his house rent allowance (HRA) under the Income Tax Act he stays in a rented house. HRA is the amount paid by the employer to the employee as a part of his salary package. HRA is given to meet the cost of rented accommodation taken by the employee. Exemption of HRA is considered under Section 10(13A) of the Income Tax act and Rule 2A of the Income tax Rules.

30 Times Property Legal issues, 2009, Times of India, Bangalore Delhi  p.18.
Conditions

a. Rent must be actually paid by the assessee for the rented premises which he occupies.

b. The rented premises must not be owned by him.

iv. Home Loan Interest and Tax Deduction

The Income Tax Act offers incentives to encourage people to invest in a house. The incentives are available by way of a deduction on interest payments on the amount borrowed to purchase or construct the house. Section 24 of the Income Tax Act contains provisions relating to deductions on income from a house. Under this Section, the interest paid on a housing loan is eligible for deduction. The interest is allowed as a deduction on an accrual basis i.e. on due basis, even if it is not actually paid in cash during the year.

The interest should be payable on borrowed capital and not on notional capital. The money should have been borrowed for the purposes of acquisition of property, construction of property, or repair of property. Interest paid on a fresh loan taken to repay another existing loan is also allowed. In order to claim the deduction, the assessee should furnish a certificate from the lender to whom the interest is payable on the capital borrowed, specifying the amount of interest payable.

In case the property has been acquired or constructed with borrowed capital, the’ interest payable on the capital borrowed for the period prior to the previous year in which the property has been acquired or constructed is also eligible for deduction. The amount is deductible in five equal instalments commencing from the previous year in which the house is acquired or constructed. The first instalment is deductible in the year in which the construction of the property is completed or the property is acquired, and the balance four instalments in the four subsequent years. This is irrespective of the number of months that have elapsed during the financial year. Even if one day is left during the year, deduction for the full year is allowed.

The maximum amount of deduction eligible is Rs. 1.5 lakhs. The money should have been borrowed on or after April 1, 1999 for the acquisition or construction.
Such acquisition or construction should have been completed within three years from the end of the financial year in which the capital was borrowed. The lender needs to certify that the interest is payable for the loan advanced for acquisition or construction of the house.

The deduction amount is restricted to Rs. 30,000 in case the money has been borrowed before April I, 1999.

The date of commencement of construction is of no consequence. What is important is the construction should be completed within three years’ from the end of the financial year in which the money has been borrowed. Further, it is not required that the entire cost should be financed through a loan. Any part of the cost of the house can be financed through the loan. For tax planning purposes, it is advisable to borrow and build or purchase rather than use your own resources because in case you use your own resources no tax incentives are available.

**Joint Ownership of Property**

Joint ownership is when two or more persons hold title to the same property. In case of co-parcenary, the members have common and an equal interest in the ancestral property. Any co-owner can transfer his share in the property to an outsider or another co-owner, and the transferee steps into the shoes of the co-owner. The transferee becomes the co-owner.

A co-owner is entitled to three essentials of ownership right to possession, right to use and right to dispose off the property. Therefore, if a co-owner is deprived of his property, he has a right to be put back in possession. Such a co-owner will have an interest in every portion of the property and has a right irrespective of his quantity of share, to be in possession jointly with others. This is also called joint-ownership.

Co-ownership can be changed to sole ownership through partition. The term co-owner is wide enough to include all kinds of ownerships such as joint tenancy, tenancy in common, co-parcenary, membership of Hindu Undivided Family etc. The very fact that the parties have certain shares in the property indicates that they are co-owners.

**Right of Survivorship**

Upon the death of one joint tenant, his interest immediately passes to the surviving joint tenants and not to the descendant’s estate. Joint tenants hold a single unified
interest in the entire property. Each joint tenant must have an equal share in the property. Each joint tenant may occupy the entire property subject only to the rights of the other joint tenants.

Joint tenancy has several requirements that must be met in order to be properly created. The conveyance must state specifically that the grantees are taking the property jointly. There are four additional legal requirements necessary in order to create a joint tenancy. Unity of time: The interests of the joint tenants must vest at the same time. Unity of possession: The joint tenants must have undivided interests in the whole property and not divided interests in separate parts.

**Unity of title:** The joint tenants must derive their interest by the same instrument. Unity of interest: Each joint tenant must have estates of the same type and same duration. All these four unities must exist. If one unity is missing at any time during the joint tenancy, the type of co-ownership automatically changes to a tenancy in common. A joint tenancy may be created by a will or deed but can never be created by intestacy because there has to be an instrument expressing joint tenancy. A joint tenancy is freely transferable.

**Tenancy by Entirely**

This type of co-ownership is exclusively for a husband and wife. Tenancy by entirety provides the right of survivorship. To exist, a tenancy by entirety requires that the four unities of a joint tenancy exist, plus a fifth unity of marriage should exist between the two co-owners. However, even if all five unities exist, the type of co-ownership may still be joint tenancy if the conveying instrument indicates as such. Unlike joint tenancy, tenancy by entirety does not allow one spouse to convey his or her interest to a third party. However, one spouse may convey his or her interest to the other spouse. A tenancy by entirety may be terminated only by divorce, death, or mutual agreement by both spouses. A terminated tenancy by entirety becomes a tenancy in common.

The Transfer of Property Act 1882 deals with transfer by a co-owner. It also deals with the rights of a transferee in this type of a transaction. Where a co-owner transfers his share of a property, the transferee acquires the transferor’s right to joint possession, use, and to enforce a partition of the property. Where the transferee of a

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31 The Transfer of Property Act 1882, section 44.
share of a house belonging to an undivided family is not a member of the family, he will not be entitled to joint possession or other uses.
A person who takes transfer from another, steps into the shoes of his transferor, gets all the rights, and becomes subject to all the liabilities of the transferor. He becomes as much a co-owner as the transferor was before the transfer. A coparcener of a Hindu Undivided Family can alienate his share in the property for a consideration. But-in some cases of Mitakshara coparcenary, the consent of other coparceners is required before any such transfer.

**Tenancy in Common**
When the type of co-ownership is not specifically stated, by default a tenancy in common is likely to exist. Each tenant in common has a separate fractional interest in the entire property. Although each tenant in common has a separate interest in the property, each may possess and use the whole property.
Tenants in common may hold unequal interests in the property but the interest held by each tenant in common is a fractional interest in the entire property. Each tenant may freely transfer his interest in the property. Tenants in common do not have the right of survivorship. Therefore, upon the death of one tenant in common, his interest passes through a Will or through the laws of intestacy to another person, who will then become a tenant in common with the surviving co-owners.

**v. Joint Loan and Tax Benefits**
While purchasing property, one can opt for a joint loan with your spouse. In case both husband and wife are working or have separate sources of income, they can go in for a joint loan. This way the loan amount also increases. Under the Income Tax Act, tax benefits are available on home loans and the interest paid on them. In case of joint loans also, all the co-borrowers can get tax benefits. A bit of documentation and planning can go a long way in avoiding hassles at a later stage. One can also take the maximum advantage of the available tax provisions and benefits.
It needs to be ensured that both should be co-owners of the property. A co-owner of a house must be a co-borrower as well. It is essential for a co-borrower to be a co-owner in order to claim the tax benefits. One cannot get tax benefits if he is only a co-borrower and not a co-owner too.
Co-borrowers, who are also co-owners: are eligible for the tax rebate in the proportion of their share in the loan. The repayment capacity of each spouse will be taken into account while arriving at the share of the loan. The shares of the loan may be in any ratio. The tax benefits would be shared in that proportion only. You have to specify the share of the property and other loan details on a stamp paper:

In case a husband and wife pay Rs. 1 lakh as interest and Rs. 25,000 as principal, each has an equal share in the borrowing, and each can claim Rs. 50,000 towards interest and Rs. 12,500 towards principal in their respective income tax returns. The maximum tax deduction for a single borrower is Rs. 1.5 lakhs. This deduction would apply to each borrower.

In case one of the co-owners does not have any income, the other co-owner should enter into an agreement with the spouse. The agreement should state that the entire repayment is met by only one borrower’s income. This would ensure that the main applicant will have 100 percent beneficial home ownership, and consequently, he can avail all the tax benefits applicable to a single borrower.

As far as repayment of the loan is concerned, it may be repaid from a joint bank account, where both the husband and wife share funds. Another option, although less popular, would be to share out the EMIs between the husband and wife, and both issue a specified number of cheques towards the loan repayment. It would need to be ensured that the repayment of the loan is made in the same ratio as the joint borrowing. Further, each of the borrowers should have a demonstrable source of income to justify the repayment of loan.

Each borrower needs a copy of a borrower’s certificate. It has to be provided to claim their respective tax relief. A co-borrower should enter into a simple agreement with the spouse on a Rs. 100 stamp paper. This agreement should basically contain the shares of the ownership along with that of the home loan availed by the couple. The borrowers should take two copies of the interest and principal paid certificates from the bank and each can submit a copy of the certificates along with a copy of the agreement signed between them.
vi. Property Gift Deed Registration Mandetory

Gift refers to the transfer of certain existing moveable or immoveable property by one person to another. A gift is a transfer without any element of consideration. Love, spiritual benefit and many other such emotions may be the intention of the donor to make a gift. Complete absence of monetary consideration is an important prerequisite. Where there is any equivalent of benefit measured in terms of money in respect of a gift, the transaction ceases to be a gift.

The transfer should be made voluntarily and without consideration. The person transferring the property is called the donor. The person to whom the property is transferred is referred to as the donee. The donee must accept the property during the lifetime of the donor and while he is still capable of giving. In case the donee dies before acceptance, the gift is void. A gift can be effected through a gift deed.

Any person who is competent to contract can gift his property. A minor, being incompetent to contract, is incompetent to transfer property. A gift by a minor is void. However, a minor can accept gifts. A guardian can accept a gift on behalf of a minor containing a condition that a person nominated in the gift deed will act as a manager of the gifted property. Such acceptance would amount to recognition by the guardian of the nominated person as the manager or the agent of the minor for the purpose of such property.

A minor may be a donee. But if the gift is onerous, Onerous gift refers to a gift that is subject to conditions. These conditions are imposed on the recipient of the gift. Sometimes, onerous gift takes the nature of a sale because it involves the element of consideration the obligation cannot be enforced against him while he is a minor. But when he attains majority he must either accept the burden or return the gift. Gift may be accepted by or on behalf of the donee. Donee may be a person unable to express acceptance. A gift can be made to a child and could be accepted on its behalf. The donee must be an ascertainable person. The subject matter of the gift must be certain existing movable or immovable property. It may be land, goods, or actionable claims, and must be transferable. There cannot be any gift of future property.

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32 Transfer of Property Act, 1882, section 123.
A gift must be of tangible property. A person should be an adult and of sound mind to make a gift. A gift, to be valid, must be made by a person with his free consent and not under compulsion. However, a mere weakness of the intellect would not be sufficient to invalidate a gift if the donor could comprehend the transaction. A transfer of property in case of gift must be voluntary and made gratuitously. It must satisfactorily appear that the donor knew what he was doing and understood the contents of the instrument and its effect and also that undue influence or pressure was not exercised upon clear intention to make a gift.

Gift involves the process of giving and taking, which are two reciprocal acts. There must be acceptance of gift as well. There is no particular mode of acceptance. The acceptance may be express or implied. Further, the property must be accepted by the donee during the lifetime of the donor. Fact of acceptance can be established by different circumstances such as donee taking a property or being in possession of deed of gift alone.

Even when a gift is made by a “registered instrument, it has to be accepted by or on behalf of the donee to make it complete, failing which the gift will be bad. The law requires acceptance of the gift after its execution, though the deed may not be registered. The acceptance may be signified by an overt act such as the actual taking of possession of the property, or such acts by the donee as would in law amount to taking possession of the property where the property is not capable of physical possession. Delivery of possession is an essential condition for the validity of the gift. However, it is not necessary that in every case there should be a physical delivery of possession. Possession the delivery of which would complete a gift may be either actual or constructive. The donor should divest himself completely of all ownership and dominion over the subject of the gift.

A gift of immovable property can be made only by a registered instrument. A gift of immovable property, which is not registered, is bad in law and cannot pass any title to the donee. Documents should be stamped and registered as required, and attested by two witnesses. Mere delivery of possession without a written instrument cannot confer any title. A deed cannot be dispensed with even for a property of small value.
Acceptance - In order to constitute a valid gift, the pivotal requirement is acceptance thereof. No particular made of acceptance is required, and the circumstances throw light on the aspect. A transaction of gift in order to be complete must be accepted by the done during the lifetime of the donor. Factum of acceptance can be established by different circumstances such as done taking a property, or being in possession of deed of gift alone. If a document of gift after its execution or registration in favour of done is handed over to him by the donor which he accepts, it amounts to a valid acceptance of gift in law. The specific recital in the deed that possession is given, or delivery of duty executed instrument of gift, raises a presumption of acceptance. However, once it is found that the gift was accepted and the truth of the contents of the gift deed was admitted, clinching evidence is required to establish that the done still retained possession with him, and the document was not acted upon.

Where a father made a gift to his daughter and on acceptance by her, she allows her father to enjoy the income from properties settled in view of the relationship of father and daughter between the donor and the done, it could not be said that there was no acceptance of gift by the done even assuming that the possession of the gifted property is not absolute requirement, for the completeness or the validity of the gift as found in Muslim Law of gifts.

Signed by or on behalf of Donor- The gift deed must be signed by the donor, and a deed signed by the intended done will not effect a transfer. It is curious that while the section 123 of the Transfer of Property Act, 1882 uses the world ‘signed by or on behalf of the donor’, yet in the case of mortgages (section 59 of the TP Act) the words are ‘signed by the mortgagor’. There is, however, no significance in this distinction, and the words ‘on behalf of are mere surplusage, for where a party is illiterate, another person may with his consent sign his name for him.

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33 Transfer of Property Act 1882, section 22.
35 Nanak Chand v. Amilal, 2003 (3) RCR (Civil) 260 (P&H).
40 Sasi Bhushan v. Chandra Peshkar, (1906) ILR 33 Cal 861.
Registration- The word ‘registered’ in this section does not mean registered in the lifetime of the donor. If the other conditions to the validity of the gift are complied with, neither the death of the donor, nor his expenses revocation is a ground for refusing registration.\(^41\) When a gift of an amount is made by a promissory note which is registered, the gift is valid and complete.\(^42\)

Gift of existing and future property (section 124 of the TP Act)- There can not be a gift of future property,\(^43\) for such a gift can only be promise, and a promise not supported by consideration is invalid as contract. Accordingly, the definition in section 122 of the TP Act is limited to existing property. In a sale or mortgage, there is consideration, and so an assignment of future property by way of sale or mortgage operates as contract.\(^44\) However, a deed of gift of existing property is not invalid as to that property, because it also professes to include future property. Similarly, an unregistered deed of gift of actionable claims and immovable property was held to be valid as to the former, but void as to the latter.\(^45\) There cannot be a gift of future property either under Hindu or Muslim Law.

Revocation of gift- There is no scope in the normal course for revocation of a deed of gift when the said deed is executed by the donor, accepted by the donee, and registered by the registering authority. A deed of gift can be revoked if there is a prior condition that the gift can be revoked, or if the deed of gift has been executed under undue influence, or if donee commits fraud.\(^46\) A gift may be revocable on a condition subsequent not depending upon the will of the donor or it may be revocable on grounds which would justify rescission in the case of a contract. However, it can not be revoked for any other reason, for as already explained, a gift revocable at pleasure is no gift at all. In *Behri Lal ghose v. Sindhubala Dasi*,\(^47\) The Calcutta High Court said that the third paragraph in section 126 of the TP Act, a gift can not be revoked.\(^48\)

\(^{41}\) Kalyanasunderam v. Karuppa, (1927) ILR 50 Mad 193.
\(^{42}\) A Krishnan Aiyer v. Lakshmi Amma, AIR 1950 Tr & Coch. 73.
\(^{43}\) Brindabibi Behari v. Oudh Behari, AIR 1947 All 179.
\(^{45}\) Perumal v. Perumal, (1921) ILR 44 Mad 196.
\(^{46}\) Balai Chandra Parui v. Durga Bala Dasi, AIR 2004 Cal 276.
\(^{47}\) (1918) ILR 45 Cal 434, p.438.
\(^{48}\) Villers v. Beamont (1682) I Vem 100; Slater v. Burnley Corporation, (1888) 59 LT 636.
**Incomplete Gift**- The rule that a gift can not be revoked except on the grounds mentioned in section 126 of the TP Act does not apply to an incomplete gift. An incomplete gift can be revoked at any time.\(^{49}\) The Rangoon High Court has held that when a done is in possession under a gift incomplete for want of a registered deed, the donor may be stopped from denying the donee’s title.\(^{50}\) A gift is effective, but can not be enforced until the deed is registered.\(^{51}\) A cheque is an order to the donor’s bankers which is revoked by the donor’s death, but it is not revoked by the donor’s death if it was presented in the donor’s lifetime, and funds were appropriated by the bankers to meet it.\(^{52}\)

**Mahomedan Gifts** (section 129 of the TP Act)- No provisions of the section 129 of the TP Act applies to Mahomedan gifts.\(^{53}\) Thus, the assignment of land by a Mahomedan bridegroom in favour of his bride at the time of marriage in lieu of *meher* does not require writing.\(^{54}\) “Hiba” or gift under Mahomedan law is a transfer of property made immediately and without any exchange by one person to another, and accepted by or on behalf of the latter. By virtue of section 129 of TP Act, the chapter does not affect any rule of Mahomedan law and, therefore, “hiba” or subject matter of whatever value need not be registered as required by section 123. It can be oral but it should be adequately proved.\(^{55}\)

**Gift Tax in India**

Gift tax in India is governed under the Gift Tax Act constituted on April 1, 1958. As per the Gift Act 1958, all gifts in excess of Rs. 25,000, in the form of cash (including draft / cheque), received from one who does not have blood relations with the recipient, were taxable.

However, with effect from October 1, 1998, gift tax got demolished and all the gifts made on or after the date were free from tax. But in 2004, Gift Tax was again revived partially and a new provision was introduced in the Income Tax Act, 1961 unde section 56 (2). According to this, any gifts received by any individual or Hindu Undivided

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\(^{49}\) *Standing v Bowring*, (1885) 31 Ch D 282. P 290 (CA).

\(^{50}\) *Ma Shin v. Maung Hman*, (1923) ILR 1 Rang 651.

\(^{51}\) *Kalyansunderam v. Karuppa*, (1927) ILR 50 Mad 193.

\(^{52}\) *Tae v. Leithead*, (1854) Kay 658.


\(^{54}\) *Jaitunbi Fatrubhai v. Fatrubhai Kasambhai & others*, (1947) ILR Bom 37.2.

Family (HUF) in excess of Rs. 50,000 in a year would be taxable (there are exceptions to this which we will deal with subsequently).

**Exemption from Gift Tax**

In the following case, the receiver will be exempt from applicable gift tax:

1. The gift being given by a blood relative, irrespective of the gift value.
   Immovable properties located outside the country.
2. Gifts received from relatives on the occasion of marriage (including gifts received by daughter-in-law from parents-in-law; but excluding gifts received by son-in-law from parents-in-law).
3. Gifts received by way of a will and inheritance.
4. NRIs gifting parents in India from their NRE account

**Defining of Relatives**

The definition clarifies the term relative to ensure that there are no loop holes which could in turn lead to some sort of money laundering. The relations who would come under the ambit include:

1. Spouse of the individual.
2. Brother or sister of the individual.
3. Brother or sister of the spouse of the individual.
4. Brother or sister of either of the parents of the individual.
5. Any lineal ascendant or descendant of the individuals.
6. Any lineal ascendant or descendant of spouse of the individuals.
7. Spouse of the Brother / sister of individual or brother/ sister of spouse of individual

**Gifting Minors & Realty**

Even gifts received by minors will be brought within the purview of taxes by means of clubbing of income, in case of both parents having taxable income, it will be clubbed with the parent who is earning the highest.

Real estate deals done for values lower than the rates fixed by state governments / local bodies will also be taxed. Here, the tax will be levied on the difference of amount between state government’s rate and purchase price. The tax needs to be paid by the buyer of the property.
An effective curb against money laundering

It was found that many individuals used the loopholes in this act, to launder money. The key reason for bringing back Gift Tax in its latest avatar is to plug loopholes and make norms more stringent. It is clear that exchanging assets amongst relatives to evade taxes have come under control and this has also ensured that the Income tax authorities can keep tab on the movement of assets (movable / immovable).


Gift means transfer by one person to another of an existing movable or immovable property made voluntarily and without consideration in cash or kind, and includes deemed gifts, as provided in the Gift Tax Act, 1958 (“the Act”).

Gift tax is charged in respect of gifts made by a person during the year. Most of the definitions given in the Act are same as those under the Income Tax Act. For definitions, refer to The Basics of Income Tax Laws.

Before making a gift, you are advised to carefully go through the list of exemptions given in the later part of this page to ascertain whether the gift falls under the exempt category. If the gift proposed by you is not exempt, gift tax is payable by you. Gift tax is payable by the donor, and not by the donee. A basic exemption of Rs. 30,000 is allowed and the amount over and above this exempt limit of Rs. 30000 is put to tax @ 30%. An incentive is provided if the tax is paid within 15 days of making the gift.

Gifts Exempt: Following gifts made by any person are exempt from tax:

1. Gifts of immovable properties situated outside India.
2. Gifts of movable properties outside India, unless the donor-
   i. being an individual, is a citizen of India and is ordinarily a resident of India, or
   ii. not being an individual, is Indian resident during the year of gift.
3. Gift of foreign currency by an NRI to a resident relative, of convertible foreign exchange, remitted from abroad.
4. Gift by an NRI out of the balance in his Non-resident (External) Account.
5. Gift of a foreign exchange asset by an NRI to a relative.
6. Gifts of Savings Certificates issued by the Central Government, which the Government notifies as exempt.
8. Gifts of Capital Investment Bonds by an individual or an HUF subject to a maximum limit of Rs. 10,00,000 per year.
9. Gift of Relief Bonds by the original subscriber to such bonds who is an Individual or an HUF.
10. Gift by an NRI of certain bonds specified by the Central Government, which have been subscribed in foreign currency.
11. Gift to any Government or any local authority.
12. Gift to any fund or institution established for charitable purpose.
13. Gift to any notified gurudwara, temple, mosque, church or any other place of worship.
14. Gift not exceeding Rs. 1,00,000 to a dependent relative, on the occasion of marriage of such relative.
15. Gift under a will.
17. Reasonable gift to children for their education.
18. Reasonable gift of bonus, gratuity, or pension by an employer to an employee or the dependants of a deceased employee.
19. Gift to any person in charge of Bhoodan or Sampattidan movement as the Central Government may notify.

**Gift Tax Withdrawn**

The fourth round of changes to the Union Budget have brought great relief to the taxpayers. The biggest gift came in the form of withdrawal of tax on gifts completely. As per the earlier proposal, the tax was shifted from the donor to the donee. For my analysis of the proposal. Time and again we had been representing to the Government that the administrative cost of collecting tax on gifts was more than the revenue generated from it. The Finance Minister has been bold enough to scrap the tax altogether now. Life is really going to be so easy after the repeal of the Gift Tax Act.

Example: Mr. M. N. Sethi is an NRI with relatives in India. Owing to a flourishing business Mr. Sethi is interested in gifting a house in India to his nephew. However, he is not sure about the taxation on such a transaction owing to his NRI status. Let’s take this
as an example to learn more about taxes associated with such a transaction with regard to NRIs. No special permission is required for an Indian citizen residing outside India to acquire (by purchase or gift) any immovable property in India other than agricultural land, plantation property or a farmhouse. Therefore, Mr. Sethi can buy a house in India as easily as any resident Indian. Also, for an NRI, there is no permission required to transfer (whether by sale or gift) immovable property in India. One important factor to keep an eye out for is the gift tax and income tax.

Under the Gift Tax Act, 1958, gift tax was payable by the donor upto 30th September, 1998. The Gift Tax Act has been repealed with effect from 1st October, 1998 and therefore the Gift Tax is not chargeable for the gifts made on or after 1st October, 1998. However, a new provision was inserted in the Income Tax Act 1961 under section 56 (2) which provides that if the gift is received by an Individual or Hindu Undivided Family (HUF) from any relatives or blood relatives or at the time of marriage or as inheritance or in contemplation of death and the aggregate of gifts received exceeds Rs 50,000 in a year, the gift will be taxable as ‘income from other source’.

There is no restriction on gifts by NRIs to resident Indians in foreign exchange or Indian Rupees or in the form of assets – in this example, the house. All sorts of gifts from relatives (as defines under Income Tax Act) are tax free. All that is required is an offer by the donor and acceptance thereof by the receiver in black and white. To safeguard against any hassles, the receiver should request the donor for a gift and then the donor should remit the amount to the receiver. Alternatively, the donor can offer the gift. In either case, it is necessary for the receiver to accept the gift in writing (maybe through a thank you note).

Also, the provisions relating to taxation of gifts from non-relatives and non-specified persons in excess of Rs. 50,000 would be liable to income tax only when the gift is a sum of money, whether in cash, by way of cheque or a bank draft. Thus, gifts in kind such as a gift of shares, gift of land, gift of house, gift of units or mutual funds, jewellery, etc. would not be liable to any income tax at all.

Therefore, Mr. Sethi or his nephew would not pay any ‘gift tax’ or income tax for such a transaction.
How to calculate income from house property

The calculation of income from house property i.e. the rent one earn, has to be done separately for each property owned by a person. If such a calculation results in a loss, it is allowed to be set off against income from other heads. Home loan repayments are eligible for deduction for each such property.

A. Yearly rental value = 11000*12 = 132000
B. Property Tax paid to municipal authorities = 2000 (please put in your actual no. here)
C. Net rental income = A – B = 130000
D. Standard deduction @ 30% of C = 39000
E. Interest paid for borrowed capital in current FY = 480000
F. Interest paid in prev. FY @ 20% = 20% of 570000 = 114000
G. Income From house Property = C – (D +E+F) = 130000 – 633000 = -503000

Let’s say one stay in a self-owned residence and purchase another property for self-occupation. He can still get a home loan for the second house. Provided, of course, the bank feels that you have enough income to pay off both the loans. But, this time, the tax man will view it differently. This second house cannot be treated as self-occupied, since that is the status given to the first house and you can claim that status only for one house. Here is where the favour from the tax department ceases. The tax department requires that you pay tax on the notional rent on at least one of the houses.

Notional Rent

This is the rent one would have got, if he gave the house on rent.

As an owner of two homes, one can choose a self-occupied property and the other will be taxed on the basis of notional rent. He can also change his choice from year to year. The income from such a home will be calculated using the above formula. Since this house is treated as being rented out, for income tax purposes the deduction for interest is not limited to Rs 1.5 lakh in respect of loan taken for this house. The income or loss from the second house, calculated separately as above, is aggregated and the net result is the income from house property. The entire principal paid on both the loans, will be eligible for deduction under Section 80C, subject to the overall cap of Rs 1 lakh. When one own more than one house, he may also be liable to pay wealth tax, if the net value
of loan, along with other assets chargeable to wealth tax, exceeds Rs 15 lakh. Even for wealth tax purposes, the value of one self occupied house is allowed to be deducted.

### Basis of Section 22 of the Income Tax Act, 1956

The annual value of a property, consisting of any buildings or lands appurtenant thereto, of which the assessee is the owner, is chargeable to tax under the head ‘Income from house property’. However, if a house property, or any portion thereof, is occupied by the assessee, for the purpose of any business or profession, carried on by him, the profits of which are chargeable to income-tax, the value of such property is not chargeable to tax under this head.

Thus, three conditions are to be satisfied for property income to be taxable under this head.

1. The property should consist of buildings or lands appurtenant thereto.
2. The assessee should be the owner of the property.
3. The property should not be used by the owner for the purpose of any business or profession carried on by him, the profits of which are chargeable to income-tax.

### Applicability of Section 22

Buildings or lands appurtenant thereto The term ‘building’ includes residential houses, bungalows, office buildings, warehouses, docks, factory buildings, music halls, lecture halls, auditorium etc. The appurtenant lands in respect of a residential building may be in the form of approach roads to and from public streets, compounds, courtyards, backyards, playgrounds, kitchen garden, motor garage, stable or coach home, cattle-shed etc, attached to and forming part of the building. In respect of non-residential buildings, the appurtenant lands may be in the form of car-parking spaces, roads connecting one department with another department, playgrounds for the benefit of employees, etc.

All other types of properties are excluded from the scope of section 22. Rental income from a vacant plot of land (not appurtenant to a building) is not chargeable to tax under the head ‘Income from house property’, but is taxable either under the head ‘Profits and gains of business or profession’ or under the head ‘Income from other sources’, as the case may be. However, if there is land appurtenant to a house property, and it is let

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56 The Income Tax Act 1956 section 22.
out along with the house property, the income arising from it is taxable under this head. Ownership of house property. It is only the owner (or deemed owner) of house property who is liable to tax on income under this head. Owner may be an individual, firm, company, cooperative society or association of persons. The property may be let out to a third party either for residential purposes or for business purposes. Annual value of property is assessed to tax in the hands of the owner even if he is not in receipt of the income. For tax purposes, the assessee is required to be the owner in the previous year only. If the ownership of the property changes in the relevant assessment year, it is immaterial as the tax is to be paid on the income of the previous year. Income from subletting is not taxable.

Rental income of A is taxable under the head ‘Income from house property’. However, since B is not the owner of the house, his income is not taxable as income from house property, but as income from other sources under section 56 of the IT Act.

Deemed owner: The Income Tax Act, 1956 provides that, in certain circumstances, persons who are not legal owners are to be treated as deemed.

1. If an individual transfers a house property to his or her spouse (except in connection with an agreement to live apart) or to a minor child (except a married daughter) without adequate consideration, he is deemed as the owner of the property for tax purposes. However, if an individual transfers cash to his or her spouse or minor child, and the transferee acquires a house property out of the gifted amount, the transferor shall not be treated as the deemed owner of the house property.

2. The holder of an Impartible Estate is deemed to be the owner of all the properties comprised in the estate.

3. A member of a co-operative society, company or association of persons, to whom a property (or a part thereof) is allotted or leased under a house building scheme of the society, company or association, is deemed to be the owner of such property.

4. A person who has acquired a property under a power of attorney transaction, by satisfying the conditions of section 53A of the Transfer of Property Act, that is

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57 Section 27.
under a written agreement, the purchaser has paid the consideration or is ready to pay the consideration and has taken the possession of the property, is the deemed owner of the property, although he may not be the registered owner.

5. A person who has acquired a right in a building (under clause (f) of section 269UA) of the Income Tax Act, 1956, by way of a lease for a term of not less than 12 years (whether fixed originally or extended through a provision in the agreement), is the deemed owner of the property. This provision does not cover any right by way of a lease renewable from month to month or for a period not exceeding one year.

Ownership must be of the superstructure. It is not necessary that the assessee is also the owner of the land. Thus, when a person obtains a piece of land on lease and constructs a building on it, the income from such building will be taxed in his hands as income from house property.

viii. Property Used for Own Business or Profession

The owner of a house property is not liable to tax under this head if the property is used by him for his own business or profession. But the business or profession should be such whose income is chargeable to tax. Chargeability to tax does not mean that the income is actually taxed. It is possible that in a particular year the profits are not sufficient enough to attract tax liability. What it means is that the income from such business or profession is not exempt from tax. If an employer builds quarters for residential use by his employees and the letting out of these quarters is considered as incidental to his business, the income from such property is not taxable under this head, because the property in this case is considered to be used by the owner for his own business. It shall, therefore, be taxed as business income.

The above position will not change even if the buildings are let out to government authorities for locating their undertakings like Banks, Post Office, Police Station, Central Excise Office, etc., provided the dominant purpose of letting out the accommodation is to enable the assessee to carry on his business more efficiently and smoothly. Also, income from paying-guest accommodation is taxable as income from business. Where house property owned by a partner is used by the firm (neither it is let
out to the firm nor any rent is obtained for it) for its business purposes, the partner is entitled to the exemption.

The reason for this exemption is that the notional rent of property is not allowable as a permissible deduction while computing business income, if a person carries on the business or profession in his own house property. Composite rent. In some cases, the owner obtains rent of other assets (like furniture) or he charges for different services provided in the building (for instance, charges for lift, security, air conditioning, etc.), apart from obtaining the rent of the building. The amount so recovered is known as composite rent. If the owner of a house property gets a composite rent for the property as well as for services rendered to the tenants, composite rent is to be split up and the sum which is attributable to the use of property is to be assessed in the form of annual Value under section 22: The amount which relates to rendition of the services (such as electricity supply, provisions of lifts, supply of water, watch and ward facilities, etc.) is charged to tax under the head ‘Profits and gains of business or profession’ or under the head ‘Income from other sources’. If there is letting of machinery, plant and furniture and also letting of the building and the two lettings form part and parcel of the same transaction or the two lettings are inseparable, then such income is taxable either as business income or income from other sources. This happens in the case of letting out of hotel rooms, theatres, auditoriums, etc. It is commonly understood that the charges per day for a room in a hotel are not specifically for the room only. In fact, a major portion of room tariff is for the amenities and services provided in the hotel. Similar is the case where a cinema house is let out at composite rent charged for the building, furniture, machines, equipment, staff, power consumption, etc. In all such cases, the composite rent received by the owner of the property is not to be split up and nothing is taxable as income from house property.

Rental income of a dealer in house property If a person is engaged in the business of purchasing house properties with the purpose of letting them on high rents and disposing off those properties which are not profitable for this purpose, the rental income from such property will not be taxed as business income. Any rent from house property, whether received by a dealer or a landlord, is taxable under the head ‘Income from house property’. It will remain so even if the property is held by the assessee as stock-in-trade of a business or if the assessee is a company
which is incorporated for the purpose of building houses and letting them on rent.
Disputed the title of ownership of a house property is disputed in a court of law, the
decision as to who is the owner rests with the Income-tax Department. Mere existence
of dispute as to title cannot hold up an assessment even if a suit has been filed.
Generally the recipient of rental income or the person who is in possession of the
property is treated as owner.

**House Property in a Foreign Country**
A resident assessee is taxable\(^\text{58}\) in respect of annual value of a property in a foreign
country. A resident but not ordinarily resident or a non resident is, however, chargeable
under section 22 in respect of income of a house property situated abroad, provided
income is received in India during the previous year. If tax incidence is attracted under
section 22 in respect of a house property situated abroad, its annual value will be
computed as if the property is situated in India.

**ix. Property Incomes Exempt from Tax**
Some incomes from house property are exempt from tax. They are neither taxable nor
included in the total income of the assessee for the rate purposes. These are:

1. Income from a farm house [section 2(1A) (c) and section 10(1)].
2. Annual value of one palace in the occupation of an ex-ruler [section 10(19A)].
3. Property income of a local authority [section 10(20)].
4. Property income of an approved scientific research association [section 10(21)].
5. Property income of an educational institution and hospital [section 10(23C)].
6. Property income of a registered trade union [section 10(24)].
7. Income from property held for charitable purposes [section 11].
8. Property income of a political party [section 13A].
9. Income from property used for own business or profession [section 22].
10. Annual value of one self occupied property [section 23(2)].

**Let out House Property**
Income from house property is determined as under:

Gross Annual Value \(\text{x}x\text{x}x\text{x}\) Less: Municipal Taxes \(\text{x}x\text{x}x\text{x}\)
Net Annual Value \(\text{x}x\text{x}x\text{x}\) Less: Deductions under Section 24

\(^{58}\) Section 22.
Statutory Deduction (30% of NAV) xxxxxxx
Interest on Borrowed Capital xxxxxxx
Income From House Property xxxxxxx

**Determination of Annual Value**

The basis of calculating Income from House property is the ‘annual value’. This is the inherent capacity of the property to earn income and it has been defined as the amount for which the property may reasonably be expected to be let out from year to year. It is not necessary that the property should actually be let out. It is also not necessary that the reasonable return from property should be equal to the actual rent realized when the property is, in fact, let out. Where the actual rent received is more than the reasonable return, it has been specifically provided that the actual rent will be the annual value. Where, however, the actual rent is less than the reasonable rent (e.g., in case where the tenancy is affected by fraud, close relationship or such other consideration), the latter will be the annual value. The municipal value of the property, the cost of construction, the standard rent, if any, under the Rent Control Act, the rent of similar properties in the same locality, are all pointers to the determination of annual value.

**Gross Annual Value [Section 23(1)]**

The following four factors have to be taken into consideration while determining the Gross Annual Value of the property:

1. Rent payable by the tenant (actual rent)
2. Municipal valuation of the property.
3. Fair rental value (market value of a similar property in the same area).
4. Standard rent payable under the Rent Control Act. Actual Rent: It is the most important factor in determining the annual value of a let out house property. It does not include rent for the period during which the property remains vacant. Moreover, it does not include the rent that the tax payer is unable to realize, if certain conditions are satisfied. Sometimes a tenant pays a composite rent for the property as well as certain benefits provided by the landlord. Such composite rent is to be disintegrated and only that part of it which is attributable to the letting out of the house property is to be considered in the determination of the annual value.

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59 The Income Tax Act 1956,
**Municipal Valuation**

Municipal or local authorities charge house tax on properties situated in the urban areas. For this purpose, they have to determine the income earning capacity of the property so as to calculate the amount of house tax to be paid by the owner of the property. But this valuation cannot be treated as a conclusive evidence of the rental value of the property, although such valuation is given due consideration by the Assessing Officer.

**Fair Rental Value**

It is the rent normally charged for similar house properties in the same locality. Although two properties cannot be alike in every respect, the evidence provided by transactions of other parties in the matter of other properties in the neighbourhood, more or less comparable to the property in question, is relevant in arriving at reasonable expected rent.

**Standard Rent**

Standard Rent is the maximum rent which a person can legally recover from his tenant under a Rent Control Act. This rule is applicable even if a tenant has lost his right to apply for fixation of the standard rent. This means that if a property is covered under the Rent Control Act, its reasonable expected rent can not exceed the standard rent. The Gross Annual Value is the municipal value, the actual rent (whether received or receivable) or the fair rental value, whichever is highest. If, however, the Rent Control Act applies to the property, the gross annual value cannot exceed the standard rent under the Rent Control Act, or the actual rent, whichever is higher. If the property is let out but remains vacant during any part or whole of the year and due to such vacancy, the rent received is less than the reasonable expected rent, such lesser amount shall be the Annual value. For the purpose of determining the Annual value, the actual rent shall not include the rent which cannot be realized by the owner. However, the following conditions need to be satisfied for this:

- a. The tenancy is bona fide;
- b. The defaulting tenant has vacated, or steps have been taken to compel him to vacate the property.
- c. The defaulting tenant is not in occupation of any other property of the assessee; and
- d. The assessee has taken all reasonable steps to institute legal proceedings for the recovery of the unpaid rent or satisfied the Assessing Officer that legal proceedings would be useless.
x. Deductions under Section 24

Two deductions will be allowed from the net annual value (which is gross annual value less municipal taxes) to arrive at the taxable income under the head ‘income from house property’. It has to be borne in mind that the deductions mentioned here (section 24) are exhaustive and no other deductions are allowed. The deductions admissible are as under:

Statutory Deduction

30 per cent of the net annual value will be allowed as a deduction towards repairs and collection of rent for the property, irrespective of the actual expenditure incurred.

Interest on borrowed capital.

The income Tax Act 1956.

The interest on borrowed capital will be allowable as a deduction on an accrual basis if the money has been borrowed to buy or construct the house. Amount of interest payable for the relevant year should be calculated and claimed as deduction. It is immaterial whether the interest has actually been paid during the year or not. However, there should be a clear link between the borrowal and the construction/purchase etc., of the property. If money is borrowed for some other purpose, interest payable thereon cannot be claimed as deduction. The following points are to be kept in mind while claiming deduction on account of interest on borrowed capital:

1. In case the property is let out, the entire amount of interest accrued during the year is deductible. The borrowals may be for construction/acquisition or repairs/renewals.

2. A fresh loan may be raised exclusively to repay the original loan taken for purchase/ construction etc., of the property. In such a case also, the interest on the fresh loan will be allowable.

3. Interest payable on interest will not be allowed.

4. Brokerage or commission paid to arrange a loan for house construction will not be allowed.

5. When interest is payable outside India, no deduction will be allowed unless tax is deducted at source or someone in India is treated as agent of the non-resident.

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60 The Income Tax Act 1956.
Interest attributable to period prior to construction/acquisition Money may be borrowed prior to the acquisition or construction of the property. In such a case, the period commencing from the date of borrowing and ending on the date of repayment of loan or on March 31 immediately preceding the date of acquisition or completion of construction, whichever is earlier, is termed as the pre-construction period. The interest paid/payable for the pre-construction period is to be aggregated and claimed as deduction in five equal instalments during five successive financial years starting with the year in which the acquisition or construction is completed. This deduction is not allowed if the loan is utilized for repairs, renewal or reconstruction.

xi. Computation of Income from Self-Occupied House Property

The annual value of one self-occupied house property, which has not been actually let out at any time during the previous year, is taken as ‘Nil’ [Section 23(2) (a)]. From the annual value, only the interest on borrowed capital is allowed as a deduction under section 24. The amount of deduction will be:

a. Either the actual amount accrued or Rs.30,000/- whichever is less
b. When borrowal of money or acquisition of the property is after 31.3.1999 - deduction is Rs.1,50,000/- applicable to A.Y 2002-03 and onwards. However, if the borrowal is for repairs, renewals or reconstruction, the deduction is restricted to Rs.30,000. If the borrowal is for construction/acquisition, higher deduction as noted above is available. If a person owns more than one house property, using all of them for self occupation, he is entitled to exercise an option in terms of which, the annual value of one house property as specified by him will be taken at Nil. The other self occupied house property/is will be deemed to be let out and their annual value will be determined on notional basis as if they had been let out.

Annual Value of One House away from Work Place

A person may own a house property, for example, in Bangalore, which he normally uses for his residence. He is transferred to Chennai, where he does not own any house property and stays in a rental accommodation. In such a case, the house property in Bangalore cannot be used for self-occupation and notional income, therefore, would...
normally have been chargeable although he derives no benefit from the property. To save the tax payer from hardship in such situations, it has been specifically provided that the annual value of such a property would be taken to be nil subject to the following conditions:

a. The assessee must be the owner of only one house property.

b. He is not able to occupy the house property because of his employment, business etc., away from the place where the property is situated.

c. The property should not have been actually let or any benefit is derived there from.

d. He has to reside at the place of employment in a building not belonging to him.

Annual Value of a house property which is partly self–occupied and partly let out If a house property consists of two or more independent residential units, one of which is self–occupied and the other unit(s) are let out, the income from the different units is to be calculated separately. The income from the unit which is self–occupied for residential purposes is to be calculated as per the provisions of Section 23(2)(a) i.e. the annual value will be taken as nil and only interest on borrowed capital will be deductible upto the maximum limit of Rs. 1,50,000 or Rs. 30,000, as the case may be. The income from the let out unit(s) will be calculated in the same manner as the income from any let out house property. If a house property is self–occupied for a part of the year and let out for the remaining part of the year, the benefit of Section 23(2) (a) is not available and the income from the property will be calculated as if it is let out.

Some Special Provisions
Taxability of unrealized rent recovered later\(^63\). Where any rent cannot be realized, and subsequently if such amount is realized, such an amount will be deemed to be the income from house property of that year in which it is received. We have seen earlier that the basic requirement for assessment of this income is the ownership of the property. However, in the cases where unrealized rent is subsequently realized, it is not necessary that the assessee continues to be the owner of the property in the year of receipt also.

\(^62\) The Income Tax Act 1956.
\(^63\) Section 25A.
Assessment of Arrears of Rent Received

When the owner of a property receives arrears of rent from such a property, the same shall be deemed to be the income from house property in the year of receipt. 30% of the receipt shall be allowed as deduction towards repairs, collection charges etc. No other deduction will be allowed. As in the case of unrealized rent, the assessee need not be the owner of the property in the year of receipt.

House Property Owned by Co-owners (section 26)

If a house property is owned by two or more persons, then such persons are known as co-owners. Co-owners are not taxable as an association of persons. When the share of each co-owner is definite and ascertainable, it has been provided that each of the owners will be assessed individually in respect of share of income from the property. In other words, income from the property will be determined and allocated to each co-owner according to his share. When each of the co-owners of a property uses it for his residence, each of them will also get the concessional treatment in respect of one self-occupied property.

Loss from house property

If the aggregate amount of permissible deductions exceeds the annual value of the house property, there will be a loss from that property. So far as income from a self-occupied property is concerned, and in respect of a property away from the workplace, the annual value is taken at nil and no other deductions are allowed except for interest on borrowed capital upto a maximum of Rs.30,000 or Rs.1,50,000. In such cases, there may be a loss upto a maximum of Rs.30,000 or Rs.1,50,000, as the case may be. However, in respect of a let out house property, there are no restrictions on deductions and therefore, there can be loss of any amount under this head.

The loss from one house property can be set off against the income from another house property. The remaining loss, if any, can be set off against incomes under any other head like salary. In case the loss does not get wiped out completely, the balance will be carried forward to the next assessment year to be set off against the income from house property of that year. However, such carry forward is restricted to eight assessment years only.

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64 Section 25B.
xii. Home Loans Facts-Questions and Answers

1. I have already taken a home loan from Standard Chartered Bank, and am getting tax benefit. Now I plan to buy a second house at the same place. Will I get a tax benefit for the second house also? Can I claim the tax deduction for both houses?65

**Ans.** Yes. You can get tax deduction benefits on the interest and principal paid towards the loan for the second residential property as well. The popular perception is that there is an overall restriction of Rs 1.5 lakh for tax benefit on the home loan interest. This is not true. This restriction is applicable only for self occupied house property. In fact, tax deduction is available for any number of properties and is without any limit under specific circumstances. The interest payable on a home loan is not directly deductible from your salary income (or business income).

Q-2 What are Income tax benefits of taking and repaying a housing loan under EMI Plan?66

**Ans.** You will be eligible to claim both the interest and principal components of your repayment during the year.

a. Interest can be claimed as a deduction under Section 24. You can claim up to Rs. 150,000 or the actual interest repaid whichever is lower. (You can claim this interest only when you are in possession of the house)

b. Principal can be claimed up to the maximum of Rs. 100,000 under Section 80C. This is subject to the maximum level of Rs 100,000 across all 80C investments.

c. You will need to show the statement provided by the lender showing the repayment for the year as well as the interest & principal components of the same.

Q-3 If I buy a house jointly with my wife and take a joint home loan, Can we both claim income tax deduction?

**Ans.** Yes, if your wife is working and has a separate source of income, both of you can claim separate deductions in your income tax returns. The repayment of principal amount of the loan can be claimed as a deduction under section 80C up to a maximum amount of Rs.1 lakh individually by each co-owner. In cases where the house is owned


66 [www.taxguru.in/income-tax/faq](http://www.taxguru.in/income-tax/faq)
by more than one person and is also self-occupied by each co-owner, each co-owner shall be entitled to the deduction individually on account of interest on borrowed money up to a maximum amount of Rs. 1.5 lakh. If the house is given on rent, there is no restriction on this amount. Both co-owners can claim deductions in the ratio of ownership.

**Q-4 My husband and I have jointly taken a home loan. He pays 75 percent of the EMI. What will be our individual tax benefits?**

**Ans.** As you have taken a joint home loan, both of you are eligible for tax exemption for your share of the EMI paid. For claiming income tax deduction, the EMI amount is divided into the principal and interest components. The repayment of the principal amount of loan is claimed as a deduction under section 80C of the Income Tax Act up to a maximum amount of Rs. 1 lakh individually by each co-owner. The repayment of the interest portion of the EMI is also allowed as a deduction under section 24 of the Act, which is given under the head “income from house property”. In case you are living in the house for which home loan is taken, both of you shall be entitled to deduction in the ratio (3:1) on account of interest on borrowed money up to a maximum of Rs. 1.5 lakh individually. If the house is given on rent, there is no restriction on this amount and both co-owners can claim deduction in the ratio of ownership- 3:1 in your case.

**Q-5 Plan to buy a house by raising loans from friends and relatives. Will I be eligible for tax benefit from all sources?**

**Ans.** Interest payment to friends and relatives can be claimed u/s 24 but only against a certificate received from them. In the absence of the certificate, you would not be eligible for the deduction. The recipient of interest income who issues the certificate is liable to pay tax on the interest income that he receives. As far as the principal payments are concerned, they would not qualify for tax benefit as loans only from notified institutions and banks are eligible for such deductions.

**Q-6. What are the tax benefits that I can avail of for repaying a home loan?**

**Ans.** You will be eligible to claim both the interest and principal components of your repayment during the year.
a. Interest can be claimed as a deduction under Section 24. You can claim up to Rs. 150,000 or the actual interest repaid whichever is lower. (You can claim this interest only when you are in possession of the house)

b. Principal can be claimed up to the maximum of Rs. 100,000 under Section 80C. This is subject to the maximum level of Rs 100,000 across all 80C investments.

c. You will need to show the statement provided by the lender showing the repayment for the year as well as the interest & principal components of the same.

Q-7 Can I take advantage of tax benefits from a home loan as well as claim House Rent Allowance (HRA)?

Ans. If you took a home loan and are still living in a rented place, you will be entitled to tax benefit on principal repayment under Section 80C

1. Tax benefit on interest payment under Section 24
2. HRA benefit

Of course, you can claim tax benefits on the home loan only if your home is ready to live in during that financial year. Once the construction on your home is complete, the HRA benefit stops. If you took a home loan, got possession of the house, have rented it out and stay in a rented accommodation, you will be entitled to all the three benefits mentioned above. However, in this case, the rent you receive would be considered as your taxable income.

Q-8. I have a home loan in which I am a co-applicant. However, the total EMI amount is paid by me. What is the total income tax exemption that I can avail of?

Ans. Yes, you can claim income tax exemption if you are a co-applicant in a housing loan as long as you are also the owner or co-owner of the property in question. If you are only person repaying the loan, you can claim the entire tax benefit for yourself (provided you are an owner or co-owner). You should enter into a simple agreement with the other borrowers stating that you will be repaying the entire loan. If you are paying part of the EMI, you will get tax benefits in the proportion to your share in the loan.
Q-9. I have two housing loans on two different properties. Can I get tax rebate under sec 80 C of both the loans?

Ans. Yes, you can get the 80C benefit on both loans. However, the total amount that you will be entitled to will be a total of Rs 100,000 across both the homes. The interest paid on a home loan is not directly deductible from your salary income for either of your flat loans. Income from house property will be calculated for each flat you own. If either of these calculations shows a loss, this loss can be set off against your income from other heads.

As for Section 24 deduction, on your self occupied house you can take advantage of interest payments up to Rs.1,50,000. For the other property, you can claim actual interest repaid, there is no limit for the same.

Q-10. I live in Delhi in my own house. In 2007, I took a housing loan to fund the purchase of an under-construction flat in another city (Faridabad which comes under National Capital Region of Delhi but otherwise falls in Haryana). It is expected to be completed in FY13. I haven’t claimed any tax benefit so far. What happens to the loan instalments I have paid so far? Can they also be claimed for tax benefit?

Ans. According to the Income-tax Act, 1961, where the property has been acquired or constructed with borrowed capital, the interest payable on such capital for the period prior to the year in which the property has been acquired shall be allowed as deduction in five equal installments beginning from the year in which the property is acquired. Thus, the interest included in the loan installment paid by you during the construction period shall be eligible for deduction from the year in which the flat is acquired/construction is completed.

The principal amount of the loan repaid till date shall not be available as a deduction under section 80C till the time the construction of the flat gets completed. Once the flat is completed and the possession is handed over to you, you will be eligible to claim deduction for interest paid on the loan under section 24(b) and principal amount of loan under section 80C. The total amount of deduction available under section 80C shall be limited to Rs. 1 lakh. Thus, as of now, you are not eligible for any tax benefit on such loan repayments.
Things one must know about tax benefits on home loan

1. Home loan borrowers are entitled to tax benefits under Section 80C and Section 24 of the Income Tax Act. These can be claimed by the property’s owner.

2. In the case of co-owners, all are entitled to tax benefits provided they are co-borrowers for the home loan too. The limit applies to each co-owner.

3. A co-owner, who is not a co-borrower, is not entitled to tax benefits. Similarly, a co-borrower, who is not a co-owner, cannot claim benefits.

4. Housing companies usually require all co-owners to be joint borrowers to a home loan. Loan providers specify who can be a joint borrower for a home loan.

5. The tax benefit is shared by each joint owner in proportion to his share in the home loan. It’s important to establish the share for each co-borrower to claim tax benefits.

6. The certificate issued by the housing loan company, showing the split between principal and interest for the EMIs paid, is required for claiming tax benefits.

Income tax concessions to housing finance companies (eligible corporations)

Section 36(1)(Viii) in The Income- Tax Act

In terms of the above provisions in respect of any special reserve created and maintained by a specified entity (construction companies, agricultural development companies, infrastructure development companies and housing finance companies etc.), an amount not exceeding twenty percent of the profits derived from eligible business computed under the head “Profits and gain of business of profession” carried to such reserve account. As per the cases studied in the matter ineligible corporations (entities) also claim concessions under the above provisions and face the treatment by the Income Tax Law.

I. Section 36(1)(viii) of the Income Tax Act, 1961 - Financial Corporation, reserve created by – From Assessment year 1997-98 - Whether amendment to section 36(1)(viii) by Finance Act, 1997, by which creation and maintenance of reserve funds has been made a condition with effect from 1-4-1998 for availing benefit under section

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36(1)(viii), is not retrospective in operation and it shall apply in relation to assessment year 1998-99 and subsequent years.

II. Section 36(1)(viia) of the Income Tax Act, 1961 - Bad debts - Assessment year 1997-98 - Applicant claimed deduction under section 36(1)(viia)(c) by creating a reserve for bad and doubtful debts in its balance sheet - Assessing Officer disallowed deduction on ground that applicant had not made a provision for bad and doubtful debts as required by section 36(1)(viia)(c) - On facts, it was clear that intention of assessee was for deduction under section 36(1)(viia) only, though ‘provision’ was nomenclatured as ‘reserve’ - Whether even if entry was termed as ‘reserve’ which according to assessee was in pursuance of ICAI’s opinion, since nature and character of entry remained same as envisaged under clause (viia)(c) of section 36(1), it was a provision though named as ‘reserve’ - Held, yes - Whether mere debit in appropriation account would not, by itself, disentitle assessee from claiming deduction under section 36(1)(viia)(c) - Held, yes

The applicant, a public sector undertaking, is engaged in the business of providing long-term finance primarily to State Electricity Boards. It claimed deduction under section 36(1)(viii) and same was allowed in the regular assessment. Subsequently assessment order was reopened under section 147 and deduction claimed under section 36(1)(viii) was disallowed on the ground that it was mandatory for the assessee to maintain the special reserve created for the purpose of availing deduction under section 36(1)(viii) and since the assessee had subsequently withdrawn and transferred the special reserve to general reserve, the deduction already allowed was liable to be withdrawn. The applicant has sought advance ruling on question as to whether the income-tax authorities are justified in making disallowance under section 36(1)(viii) as per the provisions of that section as it stood at the material point of time.

From the provisions of section 36(1)(viii), it can be seen that while the Legislature had amended section 36(1)(viii) and intended to confer the benefit under that section only if special reserve created is maintained, the consequence of withdrawing the amount from the special reserve in the previous year is taken care of by sub-section (4A) of section 41. In other words, if any deduction has been allowed in respect of any special reserve under section 36(1)(viii) and it is subsequently withdrawn, then it shall be deemed to
have been profits and gains of the business and is chargeable to income-tax. Thus, the creation and maintenance of the reserve fund has been made a condition with effect from 1-4-1998 for availing the benefit under section 36(1)(viii) and the consequence of withdrawing any such amount after deduction is made, by fiction of law, is deemed to be the profit and gains of business chargeable to tax as the income of the previous year in which the amount is withdrawn.

Further, a comparative analysis of the provisions for two respective assessment years, i.e., 1997-98 and 1998-99 shows that under the pre-amended section 36(1)(viii), subject to certain conditions, a deduction was provided in respect of a special reserve created by a financial corporation of an amount not exceeding 40 per cent of the total income, carried to such reserve account. Crucial words in these provisions are ‘special reserve created’, ‘40 per cent of the total income’ and ‘carried to such reserve account’. With these crucial words, the section contemplated the creation of reserve out of the total income of the relevant previous year and it contemplated that the profits should be carried to such reserve account.

The material variation between the provisions as they stood in the assessment year 1997-98 and the assessment year 1998-99 is that of insertion of the word ‘and maintained’ with effect from 1-4-1998, i.e., applicable from the assessment year 1998-99. The amendment has been effected primarily to incorporate the condition regarding maintenance of reserve and seems to have been necessitated to overcome some deficiencies in the Act, such as likely misuse of the provision. An amendment to section 41, i.e., insertion of clause (4A) has also simultaneously been made in order to bring to tax any amount withdrawn from such special reserve in the year in which the amount is withdrawn.

Clause (viii) of section 36(1), as it stood before amendment, cannot construed as to imply an obligation to maintain the special reserve intact. It would amount to reading words which were not there in the pre-amended provision. The importance of difference between the expressions ‘created’ and ‘maintained’ cannot be understated. But for the amendment, the restriction against withdrawal of special reserve cannot be read into the main clause (viii). The Legislature having noticed the need for amendment so as to prevent its misuse or to carry out the objective in a more effective manner, thought it fit
to introduce the word ‘maintain’ while at the same time amending section 41 in order to ensure that the amount withdrawn from the special reserve is subjected to tax. Thus, the Finance Act, 1997 has brought into existence a new scheme of taxation. It cannot be said to be just a reiteration of the old provision. True, the main provision as well as the proviso should be read together and if possible be so construed as to promote the objective of the proviso, but it cannot be done in the absence of clear words and in the absence of ambiguity in the pre-existing provision. The apprehension expressed by the revenue that unless the requirement of maintenance of special reserve created is implied, the second proviso will be a dead letter does not appeal. The diversion from special reserve need not always be there to circumvent the second proviso. Various business exigencies or considerations may weigh with the assessee in deciding upon withdrawal from special reserve. It need not always be viewed from taxation angle. For instance, in the instant case, the applicant had still maintained a substantial part of the special reserve even after transferring a part of it to the general reserve. Assuming that the effective working of the second proviso is impaired if the special reserve is not required to be maintained intact, the remedy lay in legislative amendment and that is why the Legislature stepped in to introduce the amendment without giving retrospective effect to the same. Merely because the objective of the provision will be better served, it is not permissible to read words into a provision which is otherwise clear.

It is well-settled that an amending provision is regarded as clarificatory or declaratory when the same is introduced to clear the doubts or ambiguity as regards its meaning in order to avoid unintended consequences. In the instant case, there is no ambiguity in the earlier provision of section 36(1)(viii) as the only requirement for claiming the deduction was the creation of the special reserve and the proviso was there to take care of the computational aspect. That very scheme had been existing right from the inception of the Act. Moreover, in the absence of the clear words indicating that the amendment was clarificatory, it would not be so construed when the pre-amended provision was clear and unambiguous. Where a new provision impairs an existing right or creates a new obligation, retrospectivity cannot be inferred. If the enactment is expressed in language which is fairly capable of either interpretation, it ought to be construed as prospective only.
There is no doubt that the purpose of the expression ‘and maintained’ is obviously to impose an additional obligation and it is not merely declaratory of the existing legal provision. The Legislature, by the amendment in question, seeks to restrict the benefit which the statute hitherto provided to the assessee. The scope and effect of the aforesaid amendment as also the insertion of section 41(4A) have been elaborated in the departmental circular No. 763, dated 18-2-1998.

In view of above, it emerges that the amendment takes effect from 1-4-1998 and shall apply in relation to the assessment year 1998-99 and subsequent years. [Para 20]

Therefore, the income-tax authorities were not justified in making/confirming the disallowance under section 36(1)(viii) as per provisions of that section as it stood at the material point of time.

The assessee, a public sector undertaking, is engaged in the business of providing long-term finance primarily to State Electricity Boards. For the assessment year 1997-98, it claimed deduction under section 36(1)(viia)(c) by creating a reserve for bad and doubtful debts. The Assessing Officer disallowed the claim on the ground that since the assessee had not made a provision for bad and doubtful debts as required by section 36(1)(viia)(c), the deduction under the said section was not allowable. The assessee has sought advance ruling on the question as to whether the income-tax authorities are justified in making the disallowance under section 36(1)(viia) in spite of the fact that reserve for the same had been created.

The assessee has contended that no adverse inference should be drawn even if it has, instead of making a provision, created a ‘reserve’ by debiting the same to profit and loss appropriation account, because the creation of ‘reserve’ had been for the specific purpose of claiming deduction under section 36(1)(viia)(c).

A look into the section 36(1)(viia)(c) shows that this clause grants deduction up to the aggregate ceiling of 5 per cent of the total income subject to the modalities of computation, to a public financial institution or State Financial Corporation or State Industrial Investment Corporation, if these entities make any ‘provision for bad and doubtful debts’. Thus, the requirement of section is that of making a provision for bad and doubtful debts and it does not enjoin that the provision is to be debited to the profit and loss account. However, as per the decision in the case of Vazir Sultan Tobacco Co.
The provision is a charge against the profits to be taken into account in the gross receipts as profits and loss account and ‘reserve’ is an appropriation of profits. When one looks into entries in the accounts of the assessee, it emerges that in the profit and loss appropriation account, the exact stipulation made reads :- ‘Reserve under section 36(1)(viia) for bad and doubtful debts’. The amount debited on that score is 4.5 crores. It is, thus, clear that the intention of the assessee was for deduction under section 36(1)(viia) only, though the ‘provision’ was nomenclatured as ‘reserve’. It is the contention of the assessee that the entry under the caption ‘reserve’ in place of ‘provision’ was made in pursuance of the opinion expressed by the Expert Advisory Committee of the Institute of Chartered Accountants (ICAI). Be that as it may, even if it is termed as reserve, which according to the assessee was in pursuance of the ICAI’s opinion, the nature and character of the entry remained the same as envisaged under clause (viia)(c) of section 36(1). In substance, it is a ‘provision’ though named as ‘reserve’. The debit in the appropriation account would not, by itself, disentitle the assessee from claiming the deduction. One has to see the substance and the real nature of the methodology adopted by the assessee. Hence, the assessee merits deduction under section 36(1)(viia)(c).

**Union Budget Speech dated 28.02.2013 (High lights of house taxes)**

**No change in personal and corporate tax rates.** Tax rebate of up to INR 2,000 per annum introduced for resident individuals, with total income up to INR 0.5 million per annum. Surcharge introduced for individuals (10 percent if taxable income exceeds INR 10 million). Surcharge on domestic companies increased to 10 percent from 5 percent and for foreign companies increased to 5 percent from 2 percent if taxable income exceeds INR 100 million. Surcharge on DDT for domestic company increased to 10 percent from 5 percent. This Addition in / increase in surcharge to be in force only for one year.

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71 The Economic Times, New Delhi dated March 01, 2013.
Sunset date for being eligible to claim tax holiday by power generating, distributing or transmitting companies extended by one more year to 31 March 2014.

Investment allowance at 15 percent on investments made by a manufacturing company in new Plant and Machinery acquired and installed between 1 April 2013 and 31 March 2015 if the same exceeds INR 1 billion.

Tax to be deducted at 1 percent on sale of Land or building exceeding INR 5 million. (Agricultural land excluded). Consideration for transfer of land and building (being stock in trade) to be taken as per stamp duty value as on date of agreement for sale.

Transaction of Immovable property by an individual or HUF for inadequate consideration to attract taxation as per stamp duty valuation. Subject to conditions, an additional one time deduction of up to INR 100,000 introduced for individuals in respect for interest payable to a specified financial institution on housing loan sanctioned in FY 2013-14. The deduction available in FY 2013-14 and to the extent unutilized in FY 2014-15.

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