Rental income earned by treating property as a capital asset would be assessable as 'income from house property'

Summary – The Mumbai ITAT in a recent case of Ismail Abdulkarim Balwa, (the Assessee) held that where assessee had earned rental income by exploiting property as a capital asset and letting out of building was not an adventure in nature of trade or business, impugned income was liable to be assessed as 'income from house property'

Facts

- The assessee along with two others acquired a plot of land. The three co-owners jointly constructed a building on the land and given it on a monthly tenancy from 1999 onwards. In none of the assessment years, any deprecation was claimed or allowed in the hands of the co-owners. On 24-9-2004, the said property being land and building along with small furniture and water pumps was sold for a consideration of Rs. 3.40 crores.
- The assessee filed the return of income and, accordingly, declared long-term capital gain on such sale of Rs. 66 lakhs after considering the cost of acquisition.
- The Assessing Officer observed that the assessee had consistently declared rental income from Immovable property as 'Income from business' because assessee was debiting various expenses pertaining to such income in profit and loss account. Therefore, the building in question was a depreciable asset and deprecation on it was allowable even though the assessee had not claimed it. Therefore, the Assessing Officer treated the capital gain arising from sale of such depreciable asset as short-term capital gain in view of provision of section 50.
- The Commissioner (Appeals) also confirmed the finding of the Assessing Officer.
- On appeal:

Held

- In the instant case, the property in question was let out in terms of a Tenancy agreement. Some of the salient features of the property and the terms of tenancy agreement are as follows. The property in question is a co-ownership property and the same has been let out to the tenant, who is using it for carrying out day-to-day business of automobile workshop, *etc.* it is also quite clear that apart from providing of right to use the property as a tenant, no other complex or specific services are being provided by the assessee-landlord. In fact, the agreement does not contain reference to any other services or amenities that are linked to the rental income which primarily relates to the usage of property by the tenant. Under these circumstances, it is a case where the assessee has earned rental income by exploiting the property as a capital asset and it is not a case where the letting out is to be perceived as an adventure in the nature of trade or business. Even otherwise, it is

well established that one is expected to look at the letting-out from the point of a businessman to find out whether the same is being carried out as an act of business or it is a mere exploitation of the ownership of the property. It is also a fact in the present case that the assessee or the other two co-owners or even the co-ownership AOP are not involved in any business activity of renting of properties or even as developers or builders. Therefore, it is a case where the income by way of rent has been earned in the course of exploitation of the ownership of property which quite clearly is liable to be assessed as 'income from house property'. Therefore, enough weight is found in the plea of the assessee that rental income derived from such property is liable to be considered under the head 'income from house property'.

- Now, take up the objections of Assessing Officer in this regard. Firstly, according to the Assessing Officer, assessee has declared the income from co-ownership of the property as 'business income'. The co-ownership has claimed certain small expenses on account of electricity charges, bank charges and insurance, *etc.* The important point is that the said mistake by the assessee is not fatal so as to prevent the income-tax authorities from revisiting the issue to find out the true nature and character of the income. On this aspect, it is a well-settled proposition that the income-tax authorities cannot merely go by the position taken by the assessee, howsoever erroneous it may be, without taking into consideration the applicable legal position. The mere factum of assessee declaring income from the co-ownership property as 'business income' is not conclusive of the head under which such income is assessable. Even otherwise, on facts also, the claim of assessee for deduction of small amounts of expenses, *viz.*, electricity charges, insurance and bank charges is not prejudicial to the interest of the revenue because if the computation was to be made under the head 'income from house property', assessee would have been entitled to statutory allowances against the rental income permissible under section 24(a) at the rate of 30 per cent, implying that the income forming part of the total income would have been even lower than what has been returned by the assessee. Therefore, there is no justifiable reason with the income-tax authorities to shut out the case of assessee to evaluate the nature of rental income as being assessable under the head 'income from house property'.
- Another significant aspect, which has been vehemently brought out by the revenue, is that the depreciation is deemed to have been allowed and, therefore, the property is to be considered as a business asset. In fact, it has been repeatedly asserted by the assessee that no depreciation claim has been made by the assessee and nor it has been allowed in any of the assessment years either in the hands of the assessee or even the other co-owners. In fact, at this stage, it would also be pertinent to refer to the status of assessment in the case of another co-owner, wherein the gain on sale of the property has been accepted by the Assessing Officer as declared by the assessee, *i.e.*, as long-term capital gain in an assessment finalised under section 143(3) for the very same assessment year of 2005-06. Thus, it is a case where similar income in the hands of a co-owner of the property has been accepted as to be assessable as Long-Term Capital Gain. Under these circumstances, the moot point is whether the revenue is permitted to adopt a contrary position, where under identical

circumstances in the case of a co-owner, the stand similar to that of assessee has been accepted? The answer is quite obvious and the need for uniformity in approach on similar issues arising in the case of different assessees by the Income-tax authorities cannot be overemphasised.

- In conclusion, therefore, stand of assessee to the effect that the rental income in question was to be treated of the nature assessable under the head 'income from house property' and not as 'business income' deserves to be accepted. As a consequence, there is no reason for the Assessing Officer to have re-characterised and recomputed the income from sale of co-ownership property as Short-Term Capital Gain by invoking the provisions of section 50. Thus, the stand of assessee is upheld and the order of Commissioner (Appeals) is set aside and the Assessing Officer is directed to recompute the income of assessee.