



Tax alert: Exemption for investment in residential house disallowed, as existing investment was in property outside India

25 October 2023

The Visakhapatnam Bench of the Income-tax Appellate Tribunal (ITAT) has held that since the taxpayer owned more than one residential house (which included a residential property outside India i.e. USA) at the time of transfer of original asset, the taxpayer was not entitled to claim the benefit of deduction under section 54F of the Income-tax Act, 1961 (ITA).

In a nutshell



Proviso to section 54F of the ITA is clear that if the taxpayer owns more than one residential house other than the new asset on the date of sale of original asset, exemption under section 54F of the ITA cannot be availed by the taxpayer.



The ITA is silent on the fact whether such residential property should be situated in India or outside India.



The Cochin Bench of the ITAT in another ruling held that the proviso to section 54F of the ITA (which contains the condition that the deduction is not available if the taxpayer owns more than one residential house) should be interpreted to mean ownership of residential houses in India.



Scroll down to read the detailed alert

Background:

- The taxpayer¹ is an individual and a resident of the United States of America (USA).
- During the Financial Year (FY) 2010-11, corresponding to Assessment Year (AY) 2011-12, the taxpayer:
 - Sold certain immovable properties and earned capital gains on the same.
 - Claimed exemption under section 54F of the Income-tax Act, 1961 (ITA) [relating to capital gains on transfer of certain capital assets not to be charged in case of investment in residential house] against such capital gains earned. The same was on the basis that, the taxpayer only owned a farmhouse and not a residential house in the US, and hence, the restriction under section 54F of the ITA of not owning more than one residential house under section 54F of the ITA, did not apply.
- Since the taxpayer did not file any return of income for the aforesaid AY, the Assessing Officer (AO) initiated reassessment proceedings. During the course of the reassessment proceedings, the AO disallowed the exemption under section 54F of the ITA since, the taxpayer already owned one residential house in the USA.
- Aggrieved, the taxpayer filed an appeal and in the course of appeal proceedings, the matter reached the Visakhapatnam Bench of the Income-tax Appellate Tribunal (ITAT).
 - The Revenue argued that that the property owned by the taxpayer in USA was not a farmhouse, but the taxpayer habitually resided in that address which was also mentioned as a residential address in the taxpayer's passport. Since the condition prescribed under section 54F of the ITA, that the taxpayer should not own more than one residential house, was not satisfied in the taxpayer's case, the benefit of section 54F of the ITA could not be granted to the taxpayer.

Relevant provisions in brief:

- [Relevant extract of section 54F of the ITA](#)

“Capital gain on transfer of certain capital assets not to be charged in case of investment in residential house.

54F. (1) Subject to the provisions of sub-section (4), where, in the case of an assessee being an individual or a Hindu undivided family, the capital gain arises from the transfer of any long-term capital asset, not being a residential house (hereafter in this section referred to as the original asset), and the assessee has, within a period of one year before or two years after the date on which the transfer took place purchased, or has within a period of three years after that date constructed, one residential house in India (hereafter in this section referred to as the new asset), the capital gain shall be dealt with in accordance with the following provisions of this section, that is to say,—

- (a) if the cost of the new asset is not less than the net consideration in respect of the original asset, the whole of such capital gain shall not be charged under section 45;
- (b) if the cost of the new asset is less than the net consideration in respect of the original asset, so much of the capital gain as bears to the whole of the capital gain the same proportion as the cost of the new asset bears to the net consideration, shall not be charged under section 45:

Provided that nothing contained in this sub-section shall apply where—

(a) the assessee,—

- (i) owns more than one residential house, other than the new asset, on the date of transfer of the original asset;...**

¹ DCIT (International Taxation) v. Babu Rajendra Prasad [2023] 152 taxmann.com 379 (Visakhapatnam-Trib.)

...and

(b) the income from such residential house, other than the one residential house owned on the date of transfer of the original asset, is chargeable under the head "Income from house property."

Decision of the ITAT:

The ITAT noted / observed as follows:

- From plain reading of the provisos (a) and (b) to section 54F of the ITA, if the taxpayer **owns more than one** residential house other than the new asset on the date of transfer of original asset, the benefit of deduction under section 54F of the ITA could not be availed by the taxpayer. The ITA is also silent on the fact whether the property should be situated in India or outside India.
- The Revenue's arguments held merit on the grounds that the taxpayer was a co-owner of the property situated in the USA which was evidenced by the property record details.
- Further, the taxpayer habitually resided in the property situated in the USA and had disclosed the address of that property in the taxpayer's passport.
- Under these circumstances, the contention of the taxpayer that the property at USA was a farmhouse could not be accepted.

In view of the above, since the taxpayer owned more than one residential house at the time of transfer of original asset, the taxpayer was not entitled to claim the benefit of deduction under section 54F of the ITA.

Comments:

The ITA provides for specific exemption to capital gains earned on sale of capital assets, other than residential house, if consideration from such sale is invested in a residential property. The same is subject to fulfilment of certain conditions such as that the taxpayer should not own more than one residential house (other than the new asset) on the date of transfer of the original asset (i.e. capital asset which is sold).

The ITAT in this ruling has rejected the taxpayer's claim of exemption under section 54F of the ITA on the basis of the taxpayer holding more than one residential property on the date of sale of capital asset, even though such property was held outside India (in USA) and held as follows:

- Proviso to section 54F of the ITA is clear that if the taxpayer owns more than one residential house other than the new asset on the date of sale of original asset, exemption under section 54F of the ITA cannot be availed by the taxpayer.
- The ITA is silent on the fact whether such residential property should be situated in India or outside India.

It is pertinent to note that the Cochin Bench of the ITAT in another ruling², held that:

- The legislative intent behind granting relief to the taxpayer through section 54F of the ITA is related to investments in residential house in India and therefore, the proviso imposing the conditions cannot be read in isolation and should be construed harmoniously with the main section.
- Accordingly, the proviso to section 54F of the ITA (which contains the condition that the deduction is not available if the taxpayer owns more than one residential house) **should be interpreted to mean ownership of residential houses in India.**

Taxpayers with similar facts may evaluate the impact of this ruling to the specific facts of their cases.

² Smt Maries Joseph v. DCIT (International taxation) [2023] 101 ITR (Trib) 629 (Cochin-Trib.)



Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee, and its network of member firms, each of which is Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee (“DTTL”), its network of member firms, and their related entities. DTTL and each of its member firms are legally separate and independent entities. DTTL (also referred to as “Deloitte Global”) does not provide services to clients. Please see www.deloitte.com/about for a more detailed description of DTTL and its member firms.

This material and the information contained herein prepared by Deloitte Touche Tohmatsu India LLP (DTTI LLP) is intended to provide general information on a particular subject or subjects and is not an exhaustive treatment of such subject(s). This material contains information sourced from third party sites (external sites).

DTTI LLP is not responsible for any loss whatsoever caused due to reliance placed on information sourced from such external sites. None of DTTI LLP, Deloitte Touche Tohmatsu Limited, its member firms, or their related entities (collectively, the “Deloitte Network”) is, by means of this material, rendering professional advice or services. This information is not intended to be relied upon as the sole basis for any decision which may affect you or your business. Before making any decision or taking any action that might affect your personal finances or business, you should consult a qualified professional adviser.

No entity in the Deloitte Network shall be responsible for any loss whatsoever sustained by any person who relies on this material.