

WEALTH TAX ON IMMOVABLE PROPERTIES

Part I : Chargeability, exclusions and exemptions

Wealth Tax as the name suggests is tax on Wealth of an assessee. However only certain assets specified in Section 2(ea) of the Wealth Tax Act, 1957 are chargeable to Wealth Tax. Wealth Tax is not payable on all assets of an assessee. Section 2(ea) is an exclusive definition and only assets specified therein are subject to Wealth Tax.

One important asset, which is subject to Wealth Tax, is any building or land appurtenant thereto which is specified in detail in Section 2(ea)(i) reproduced in Annexure I hereto.

It may be noted that only such building or land appurtenant thereto as specified in section 2(ea)(i) is chargeable to Wealth Tax. For e.g. farm house situated more than twenty five kilometers from local limits of any municipality or Cantonment Board is not chargeable to Wealth Tax. What is covered in this section is building or land appurtenant thereto. This implies that land per se is not subject to wealth tax except "Urban land" as specified in Section 2(ea)(v) of the Wealth Tax Act, 1957 read with explanation (b) thereto. It may also be mentioned here that advance for property will not fall under the purview of section 2(ea). Certain categories of buildings are specifically excluded from the charge of Wealth Tax which are stated in clause 2(ea)(i) (1) to 2(ea)(i)(5) ."

2(ea) (i)(1) : " *A house meant exclusively for residential purposes and which is allotted by a company to an employee or an officer or a director who is in whole-time employment, having a gross annual salary of less than five lakh rupees;*

As per this clause it is not necessary that such house should have been throughout the year be allotted to the employees that are specified. In between the year the house could be lying vacant or in between it may also have been allotted to the employees and other persons stated, who are drawing gross annual salary equal to or exceeding five lakh rupees. This is not stated, as a measure of planning but if inadvertently out of lapse, compulsion or otherwise if for a short span of time such house is allocated to ineligible employees the result may not be fatal. However atleast on the valuation day it may be ensured that the house is allocated only to an eligible employees. One

condition that has to be carefully considered is that the house should be meant exclusively for residential purpose.

2(ea)(i)(2) : *any house for residential or commercial purposes which forms part of stock-in-trade;*

This clause is very simple and any immovable property which forms part of stock in trade is not subject to Wealth Tax.

2(ea)(i)(3) : *any house which the assessee may occupy for the purposes of any business or profession carried on by him ;*

If an assessee is engaged in the business of letting out of houses then whether houses held by him would fall in this category of exclusion. Income earned out of business of letting out of houses shall be chargeable to tax under the head "Income from House Property" and not "Business Income". Nevertheless the head under which income is chargeable is not a criteria for determining the exclusion. What is required is user of the house for business purpose and hence if an assessee is engaged in the business of letting houses then those houses which are held for that purposes may not be chargeable to Wealth Tax. The intention seems to be this, however the things do not seem so simple. There seems to be a small hitch. The condition is not "use" of the house by the assessee for the purpose of business but "occupancy" of the house by the assessee for the purpose of business. Now when the assessee lets out house he himself cannot occupy the house. It is the lessee who shall occupy the house, strictly construed therefore houses held by an assessee for the business of letting out may not fall under this exclusion.

However such a narrow interpretation would lead to absurd results For e.g. in case of a hotel the rooms are never occupied by the owner and neither the rooms of hotel is stock-in-trade for a hotel. Does it mean that all hotels will be chargeable to Wealth Tax. This seems neither to be a correct interpretation nor the intention of law. Hence the term 'occupy' has to be given a broader meaning. To put it in brief it would mean that any Commercial premises occupied for business carried on by assessee is not an asset liable to Wealth Tax.

2(ea)(i)(4) : *any residential property that has been let-out for a minimum period of three hundred days in the previous year;*

This is a very welcome exclusion which has been inserted by Finance (No.2) Act, 1998 with effect from 1.4.99.

If suitably planned many residential properties could be saved from the net of Wealth Tax.

2(ea)(i)(5) : *any property in the nature of commercial establishments or complexes*

This insertion has also been made by Finance (No.2) Act, 1998 with effect from 1.4.99. The term "Commercial Establishment or Complexes" is a novel term. To understand the nature of exemption, Section 2 (ea)(i)(5) needs to be recapitulated in following terms:

- (a) What is taxable is any building or land appurtenant thereto used for commercial purpose.
- (b) From that, any house occupied for own business is excluded.
- (c) Even commercial premises held as stock in trade are not included.
- (d) In other words, what is taxable is commercial premises let out or commercial premises held as investment.

Out of that, now what is being excluded is a property 'in the nature of' commercial establishment or commercial complexes. The expression 'commercial establishment or complexes' have not been defined for the purpose. Accordingly, one would have to ascertain the connotation thereof or meaning thereof having regard to the normal commercial or trade understanding.

As per Black's Law Dictionary, "Commercial Establishment" would mean a place where commodities are exchanged or sold or a profit-making establishment (i.e., an establishment carrying on a business or profession). The amendment excludes any property in nature of Commercial Establishment. Now, when a place is given for use to a Trader, certainly, the place is used for a Commercial Establishment, i.e., to carry on any Trade or Business. Thus, the place is merely let out for carrying on any activity of a Commercial Establishment.

There may be cases, where a person owns a place in which he runs a Business Service Center. As a variant thereof, a person owning a place for commercial use may divide it into various Units and let them out to different persons with certain facility. In that case, the person owning could be considered as using a place as Commercial Establishment to carry on activity for profit.

The objective of the amendment is to exclude, from the purview of Wealth Tax, any premises used for productive purpose. Having regard to that in either of the above case, the place ought to be considered as Commercial Establishment.

A 'Commercial Complex' is a large building or group of buildings, which have various units for use as an office or godown or any other purpose for a commercial establishment or a business or a trade or a profession. Apart from that, in the complex various common facilities or services are available for user of an establishment, which may include any one or more of : Security, power, air-conditioning, bank or post office in the building, telecommunication facility, parking space, storage space and so on. Such complexes are built by the owners or builders and let out or given on user basis as against a lease or tenancy or by granting ownership. Such complexes are sought to be exempted. Accordingly, it seems, now what is taxable is only a vacant commercial premises held by investors.

It appears that after the above exclusion, now, what is taxable is commercial premises held by investors and not let out. In other words, apparently, only vacant commercial premises would be subjected to Wealth-Tax.

Having fallen as asset chargeable to Wealth Tax u/s 2(ea) "One house or part of a house or a plot of land belonging to an individual or HUF is exempt from Wealth u/s 5(1)(vi). It could be either a house, part of a house or plot of a land as opted by the assessee. The exemption is restricted to one unit. If there are two small eligible units of 500 sq.feet each only one would be exempt, the other would be taxable. However if there is one large unit of 5000 sq.ft. it will be fully exempt. The same would be true for a plot of land. It may be noted that as per proviso to section 5(1)(vi) no wealth tax is payable in respect of a plot of land comprising of an area upto 500 square meters. One may note here that this exemption under the proviso is not restricted only to one such plot as in the main section. 'N' number of plots of an area upto 500 square meters per plot would be exempt.

Annexure I :

"Assets", in relation to the assessment year commencing on the 1st day of April, 1993, or any subsequent assessment year, means:-

(i) Any building or land appurtenant thereto (hereinafter referred to as "house"), whether used for residential or commercial purposes or for the purpose of maintaining a guest house or otherwise including a farm house situated within twenty-five kilometers from local limits of any municipality (whether known as Municipality, Municipal Corporation or by any other name) or a Cantonment Board, but does not include-

1. A house meant exclusively for residential purposes and which is allotted by a company to an employee or an officer or a director who is in whole-time employment, having a gross annual salary of less than five lakh rupees;
2. any house for residential or commercial purposes which forms part of stock-in-trade;
3. any house which the assessee may occupy for the purpose of any business or profession carried on by him;
4. any residential property that has been let-out for a minimum period of three hundred days in the previous year;
5. any property in the nature of commercial establishments or complexes."

Part II : Valuation

Rule 3 of Schedule III is applicable only for valuation of an immovable property being building or land appurtenant thereto, on part thereof. It is not applicable for valuation of a plot of land where Rule 20 of Schedule III will be applicable.

The mode of valuation prescribed in Rule 3 to Schedule III shall not apply in following two circumstances.

1. In respect of property acquired or constructed after 31st March, 1974 where the value so arrived is lower than the cost of acquisition or the cost of construction as increased by cost of improvement if any. In such cases cost of acquisition /construction as increased by cost of improvement if any shall be taken as cost.

2. In respect of house which is acquired or constructed after 31st March, 1974 where the cost of acquisition/construction as increased by cost of improvement if any exceeds.
 - i. If the house is situated at Mumbai, Calcutta, Delhi or Madras – Rs. 50 lakhs

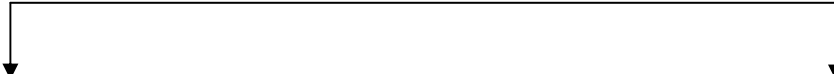
 - ii. If the house is situated at any other place Rs. 25 lakhs
In such cases cost of acquisition/construction as increased by cost of improvement if any shall be taken as cost.

Provided however that Rule 3 of Schedule III shall apply for valuation of one such house (as selected by the assessee) where such house is exclusively used by the assessee for his own residential purposes throughout the period of twelve months immediately preceeding the valuation date.

One may take a guess at the term "used by assessee for his own residential purposes throughout the period of twelve months immediately preceeding the valuation date'. Does it mean that assessee has to reside for 365 days in this house? Does it mean that he cannot even take a vacation? The term has been used very

loosely. However it would suffice if such house is actually available for residential use of the assessee for the referred period. Actual physical stay for the full period may not be required.

To summarise the above



House acquired or constructed on before 31.03.1974	House acquired or constructed after 31.03.1974.
Rule 3 method of valuing is squarely applicable to all the properties without reference to their cost	<p>Rule 3 method of valuing shall apply only if cost of such house is less than the value so arrived.</p> <p>The only concession given is that if one house belonging to the assessee which is exclusively used for his own residential purpose throughout the period of twelve months immediately preceding the valuation date and the cost of such house is less than the amounts as prescribed, then Rule 3 valuation shall be allowed only in respect of one such house.</p>

One issue that arises here is what would be the date of acquisition in respect of property acquired by way of gift or inheritance . Shall it be the day on which the property has been gifted or inherited or shall it be the day of acquisition by previous owner? There is no section in the Wealth Tax Act corresponding to section 2 (42A) of

The Income Tax Act and therefore one may conclude that date of gift or inheritance shall be treated as the date of acquisition. Now further what will be the cost in the hands of the donee or inheritor? Will it be NIL or it will be the cost to the previous owner? Again there is no section in The Wealth Tax Act corresponding to section 49 of the Income Tax Act and therefore one may conclude that cost in the hands of donee or inheritor shall be NIL. The above interpretation sometimes give an absurd result. For e.g. in case of gifted property acquired by the donor after 31.03.1974 for a cost of 1 crore would have been valued at 1 crore in the hands of the donor until it was gifted, but on gift since the cost of acquisition thereof in the hands of donee would be NIL. It will have to be valued according to formula laid down in Schedule III.

Disclaimer :

The information contained in this write up is to provide a general guidance to the intended user. The information should not be used as a substitute for specific consultations. We recommend that professional advice is sought before taking any action on specific issues.