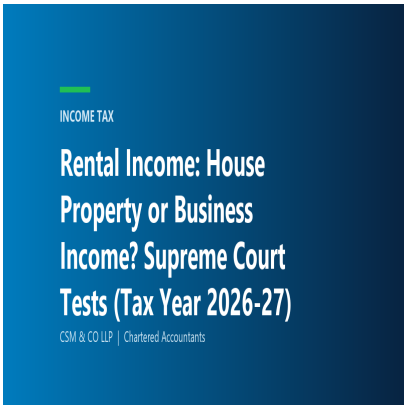

Rental Income: House Property or Business Income? Supreme Court Tests (Tax Year 2026-27)

Description

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Quick summary

- Rent from a building you own is taxed as income from house property (section 20 of the Income-tax Act, 2025), with only taxes, a flat 30% and interest as deductions.
- If letting is itself your business, the same rent can be business income, with actual expenses and depreciation allowed. This depends on facts, not on your choice.
- The Supreme Court decided this in Chennai Properties (2015), Rayala Corporation (2016) and Raj Dadarkar (2017): look at what the owner actually does, from a businessman's point of view.
- A person with long-term rights in a building, such as a lease of 12 years or more, is a deemed owner under section 25, and the rent from sub-letting can be house property income.

Rent from a property can be taxed under two heads, and they are taxed very differently. House property income allows only a flat 30% deduction, local taxes and loan interest. Business income allows the real costs of running the activity. The choice is not yours. It follows from what you actually do.

The two heads

House property (section 20). The annual value of a building and its appurtenant land that you own is chargeable to tax as income from house property, except for the part you occupy for your own business or profession. The deductions are the local taxes you paid, 30% of the annual value and interest on borrowed capital (sections 21 and 22).

Business income (section 26). Profits of a business carried on at any time in the year. If letting out property is itself a business, its profits are computed under the business provisions, with deductions such as salaries of staff, repairs, insurance, depreciation and interest, and the usual books of account.

What the Supreme Court has said

The Court looks at the **activity**, not just the ownership or the wording of a document.

Case	Facts in brief	Result
Chennai Properties and Investments Ltd v CIT (09/04/2015)	A company whose main object was to acquire properties and let them out; its only income was rent	Business income. The object clause alone is not decisive. It depends on the circumstances whether letting is the business
Rayala Corporation Pvt Ltd v ACIT (11/08/2016)	A company whose only business was leasing its property and earning rent	Business income, following Chennai Properties
Raj Dadarkar and Associates v ACIT (09/05/2017)	A partnership firm held a long-term licence over market space, built 95 shops and 30 stalls and sub-licensed them, collecting licence fees and service charges	House property income. The firm was a deemed owner; the service charges were inseparable from the rent, and it did not provide organised, systematic services

The test the Court applied in Raj Dadarkar was whether, from a businessman's point of view, the letting was the **doing of a business** or the **exploitation of property** by an owner. In Chennai Properties, where the entire income was from letting properties owned by the company, letting was the business. In Raj Dadarkar, ownership of the property characterised the activity.

A reading to avoid: some articles say Raj Dadarkar held that sub-letting as an activity makes the income business income. On its facts the Court held it was house property income.

Signs that point to business

- The **object and the main activity** of the person are letting properties, and that is the only or main source of income.
- The activity is **organised**: staff, systematic management, a range of services (not only the use of space), and books of account.
- Several properties are let continuously, and letting is exploited commercially rather than as a way of holding an asset.
- The income comes from **services** (a hotel, a hostel, a co-working space, a hall with caterers), not just the right to occupy.

Signs that point to house property

- You own one or a few properties and let them as an investment.
- The rent is for **occupation** of the building. Any service charge is a minor, inseparable part of the rent.
- The owner does no organised business activity around the letting.
- You have acquired rights in the building of the kind listed in section 25(e), such as a **lease of 12 years or more**, and you sub-let it: you are a deemed owner, so the rent is house property income. That was the basis of Raj Dadarkar, where the firm held long-term rights under a licence.

Worked comparison

A property is let at ?35,000 a month. Local taxes paid ?20,000, loan interest ?60,000.

As house property

Step	Amount (?)
Annual value (35,000 × 12)	4,20,000
Less: local taxes	20,000
Net	4,00,000
Less: 30%	1,20,000
Less: interest	60,000
Income	**2,20,000**

As business income, if letting is genuinely a business, with actual running costs of ?1,10,000 (staff ?60,000, repairs ?30,000, insurance ?10,000, depreciation ?10,000) in addition to taxes and interest:

Step	Amount (?)
Rent	4,20,000
Less: taxes	20,000
Less: interest	60,000
Less: running costs	1,10,000
Profit	**2,30,000**

The business head is not always lower: in this case the flat 30% deduction under house property is larger than the real costs. A business also brings the burden of books of account and, above the limits, audit. Do not claim a head only for the tax result.

Other points

- **Loss:** a house property loss can be set off against other income only up to ?2,00,000 in the old regime, and not at all in the new regime. A business loss is treated differently (section 109), though it cannot be set off against salary.
- **Basic exemption:** if rent is your only income, tax is nil up to the basic exemption limit of your regime,

after the deductions for the head.
- **Documentation:** keep the agreement, rent receipts, and for a business, evidence of services provided and of the staff and records.

Before you rely on this

The rulings are on their own facts and later cases apply them to different set-ups, so a case-specific opinion is worth having if the amount is large or the Assessing Officer questions your head. The sub-letting position of a deemed owner follows section 25(e) of the 2025 Act (earlier section 27(iiib)).

Frequently asked questions

Is rental income house property income or business income?

Usually house property income. It is business income only when letting is itself the business, as the Supreme Court found in Chennai Properties and Rayala Corporation, where the company's main business was letting its properties.

Does the object clause of the company decide it?

No. In Chennai Properties the Court said that an entry in the objects is not decisive; the question depends on the circumstances of each case, from a businessman's point of view.

Who decides which head applies?

The facts decide, and in a return you must report under the head the facts support. The Assessing Officer can differ. You cannot pick the more favourable head.

What deductions are allowed under each head?

House property: local taxes paid, 30% of the annual value and interest on borrowed capital. Business: expenses allowed under the business provisions of the Act (such as staff, repairs, insurance, depreciation and interest), which usually need books of account.

What did Raj Dadarkar decide?

That a partnership firm which held a long-term licence and sub-licensed shops, earning rent and service charges that were inseparable from the rent, was a deemed owner and its income was house property income, not business income.

Is sub-letting income house property or other income?

If you are a deemed owner under section 25 (for example, you hold a lease of 12 years or more), it is house property income. Otherwise it is business income or income from other sources depending on the facts.

Official sources

- Chennai Properties and Investments Ltd v CIT, Supreme Court, 09/04/2015
- Rayala Corporation Pvt Ltd v ACIT, Supreme Court, 11/08/2016
- Raj Dadarkar and Associates v ACIT, Supreme Court, 09/05/2017
- Income Tax Department: Income-tax Act, 2025 (sections 20, 21, 22, 25)

Related reading

- Decoding the Direct Tax Landscape: Budget 2025 Insights

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