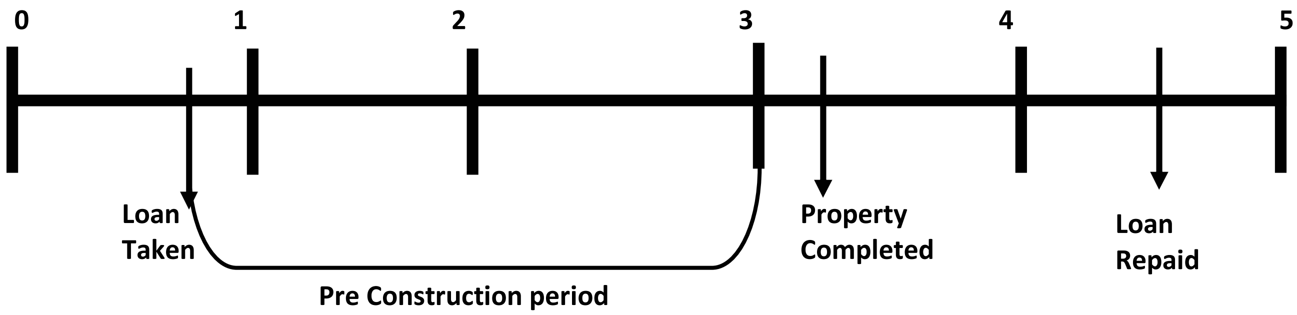
House Property

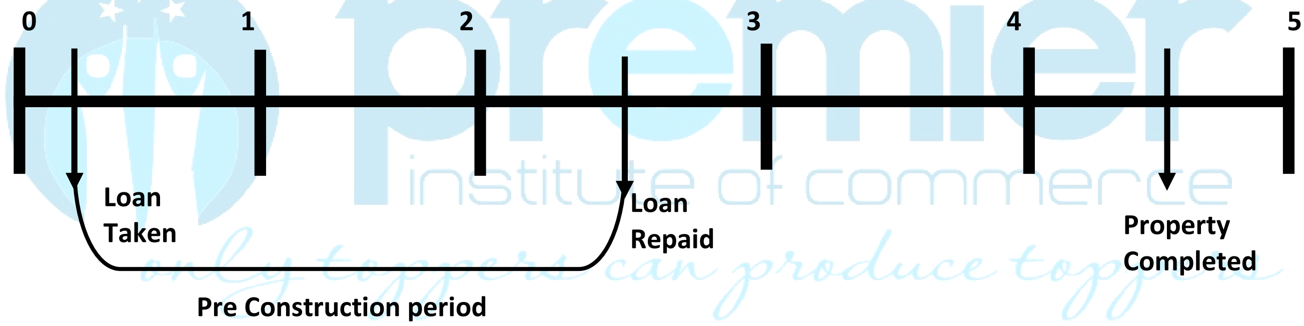
Interest on Borrowed Capital

Pre Construction Period

Case I:



Case II:



Pre Construction Interest

Interest for the period pertaining to pre construction period is called pre construction interest. This interest is allowed as deduction in five equal installment beginning with the year in which property is completed.

Current Period Interest

Current period interest will never arise in case II. In case I, Current period interest will start from first day of the year in which property is completed & will continue for each year till the Loan is repaid.

Note:

1. If capital is borrowed for the purpose of purchasing a plot of land, interest liability is deductible even if construction is financed out of own funds.
2. Interest on borrowed capital is deductible on "accrual" basis. It can be claimed as deduction on yearly basis, even if the interest is not actually paid during the year.
3. Interest on unpaid interest is not deductible.
4. No deduction is allowed for any brokerage or commission for arranging the loan.

5. Interest on a fresh loan, taken to repay the original loan raised for the aforesaid purposes, is allowable as deduction.

Illustration 1: Mr. X took a loan of ` 20,00,000 for construction of a house on 1-5-07, the property was completed on 31-12-10.

Case A: Loan was repaid on 31-3-2016.

Case B: Loan was repaid on 31-3-2013.

Case C: Loan was repaid on 31-3-2009.

Case D: Loan was repaid on 31-1-2011.

Rate of interest charged by bank is 10% pa. Compute interest to be allowed as deduction for AY 2011-12 in each of above 4 cases:

Solution:

Case A: Loan was repaid on 31-3-2016
For FY 2010-11 Current year interest = 2, 00,000
It will continue till 2015-16

Period	Interest
2010-11	2,00,000
2011-12	2,00,000
2012-13	2,00,000
2013-14	2,00,000
2014-15	2,00,000
2015-16	2,00,000

Pre Construction Period = 1-5-07 to 31-3-10
= 2 Year 11 Month

Pre Construction Interest = ` 20,00,000 X 10% X 2 + ` 20,00,000 X 10% X $\frac{11}{12}$
= ` 5,83,333

Current Year Interest = ` 20,00,000 X 10%
= ` 2,00,000

Interest on borrowed capital allowed u/s 24(b)

Pre Construction interest ` 5,83,333 X $\frac{1}{5}$	1,16,667
Add: Current Year Interest	2,00,000
	3,16,667

Case B: Loan was repaid on 31-3-2013
Same as Case A

Case C: Loan was repaid on 31-3-2009
Pre Construction Period = 1-5-07—31-3-09
= 1 Year 11 Month

Pre Construction Period = ` 20,00,000 X 10% + ` 20,00,000 X 10% X $\frac{11}{12}$

= ` 3,83,333

Interest on borrowed capital allowed u/s 24(b)

Pre Construction interest ` 3,83,333 X$\frac{1}{5}$	76,667
Add: Current Year Interest	Nil
	76,667

Case D: Loan was repaid on 31-1-2011

Pre Construction Period = 1-5-07—31-3-10

= 2 Year 11 Month

Pre Construction Period = ` 20,00,000 X 10% X 2 + ` 20,00,000 X 10% X $\frac{11}{12}$

= ` 5,83,333

Current Year Interest = ` 20,00,000 X 10% X $\frac{10}{12}$

= ` 1,16,667

Interest on borrowed capital allowed u/s 24(b)

Pre Construction interest ` 5,83,333 X$\frac{1}{5}$	1,16,667
Add: Current Year Interest	1,16,667
	2,83,334

Note: Interest is charged for the day of borrowing but not for the day of repayment.

Interest on Borrowed Capital in case of Self Occupied Property

Interest will be allowed subject to limit of ` 30,000 or ` 1,50,000. If all the following conditions are satisfied, interest will be allowed up to ` 1,50,000:

(i) Capital is borrowed on or after 1-4-1999.

(ii) Loan is taken for acquisition or construction of property.

(iii) Acquisition or Construction is completed within 3 years from the end of Financial Year in which Capital was borrowed.

If any of the above condition is not satisfied, deduction will be allowed subject to maximum ceiling of ` 30,000.

Note: When more than 1 loan has been taken, one for construction & other for renewal, total deduction for interest on all loan can't exceed ` 1,50,000 , in case of Self Occupied Property.

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