



# JB Nagar CPE Study Circle OF WIRC OF ICAI

# Accounting and Taxation Issues for Builders & Developers

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# Agenda

**1 Accounting for Real Estate Transactions- PCM vs. POCM**

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**Taxation Issues for Builders and Developers**

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**2 Valuation of Immovable Property**

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**3 Income from House Property Vs. Profits and Gains from Business and Profession**

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**4 Taxation of Notional Income**

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**5 Section 45(2) & Section 28(via)**

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**6 Joint Development Arrangements**

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**7 Redevelopment Projects and Slum Redevelopment Projects**

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**8 Budget 2021 Proposals**

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**9 Tax Impact of RERA**

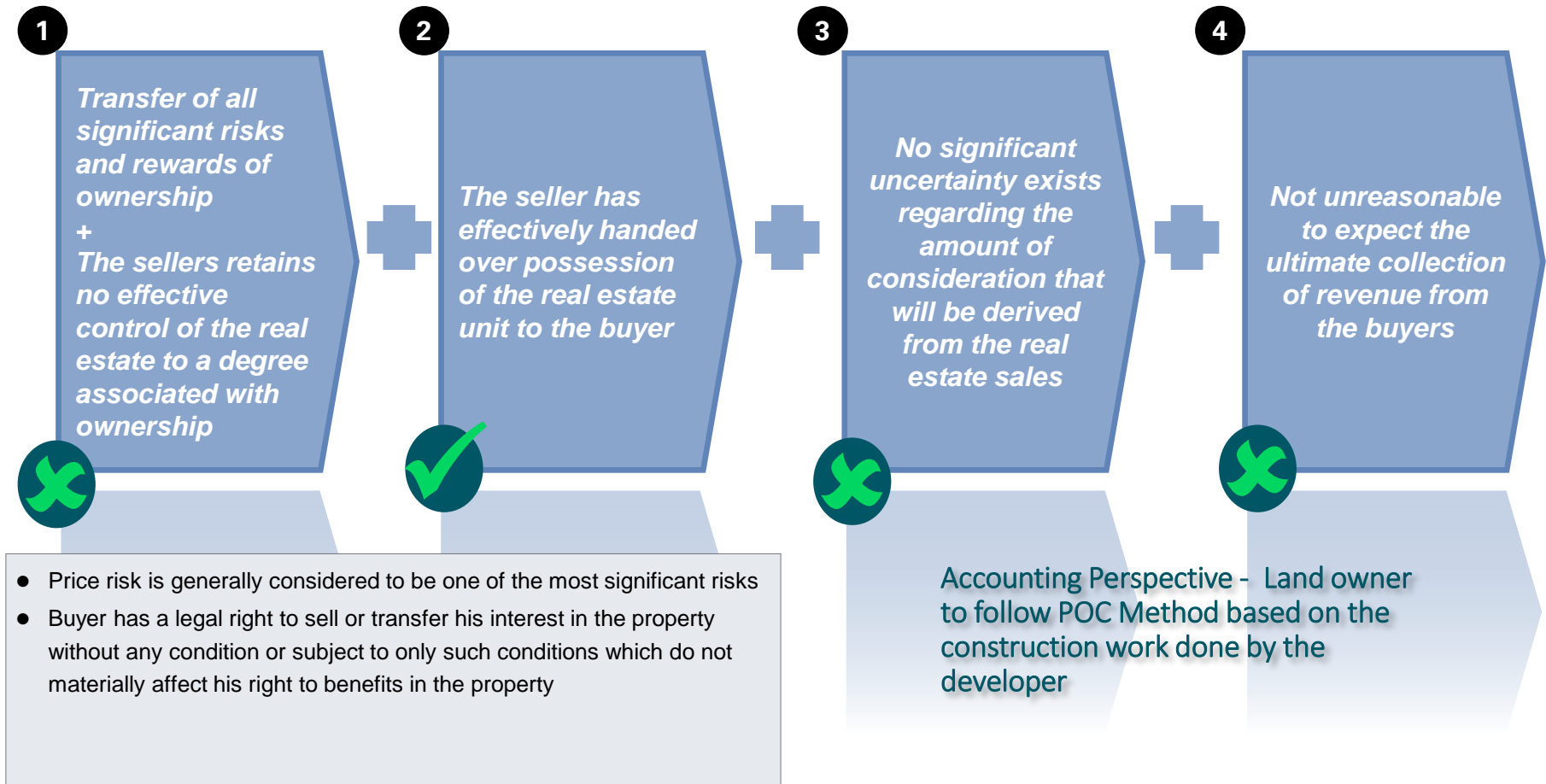
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# ACCOUNTING FOR REAL ESTATE TRANSACTIONS

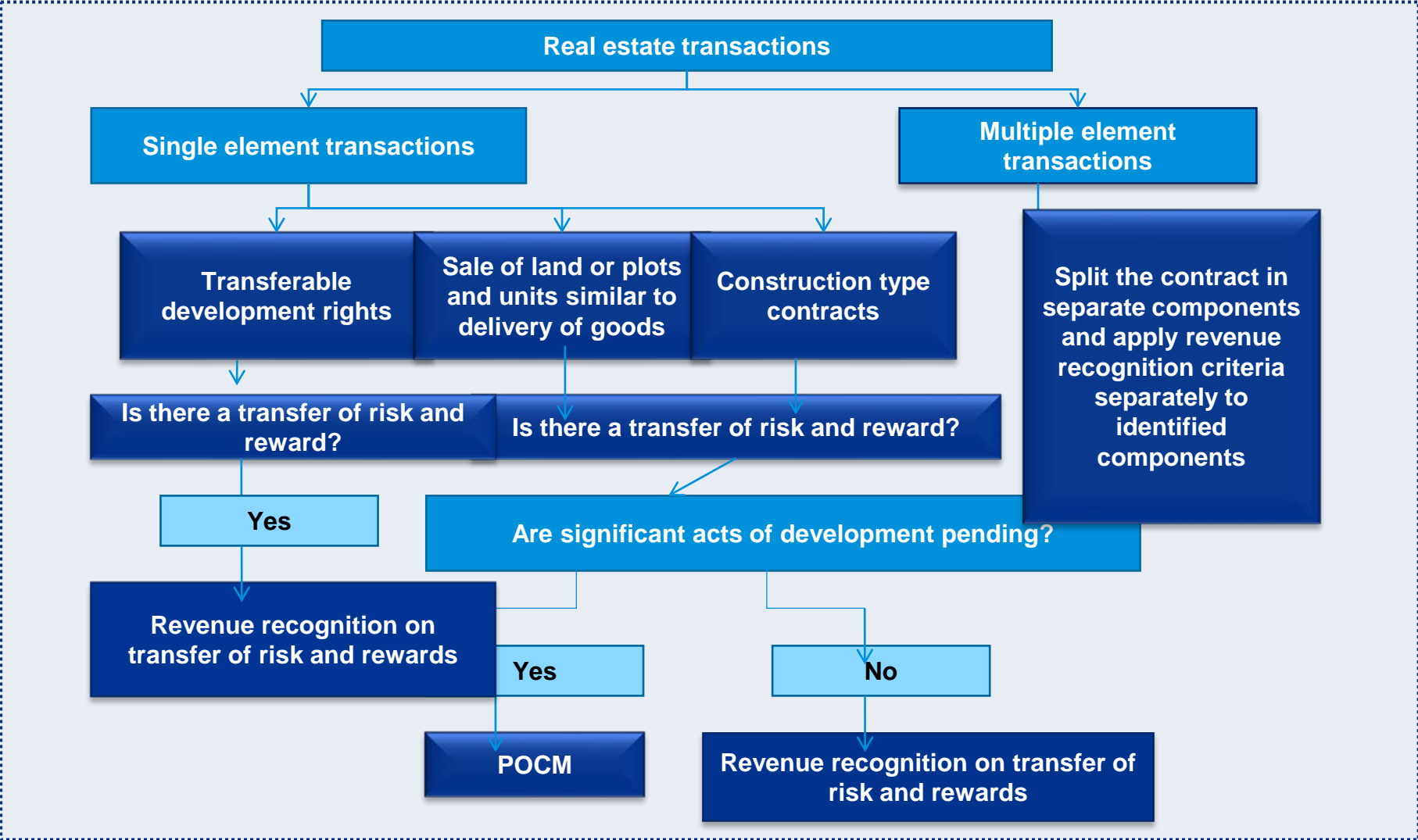
- PCM vs PCOM

# Guidance Note on Accounting for Real Estate Transactions 2012

## Para 4 of Revised Guidance Note – Application of Principles of AS 9 in respect of sale of goods to a real estate project



# Guidance Note on Accounting for Real Estate Transactions 2012



# Revised Ind AS 115

## Overall Approach

Revenue may be generated by the sale of goods, construction contracts, the rendering of services, use of entity's assets that generate fees. It is measured at the fair value of the consideration received or receivable

### Ind AS 18 Steps

Step 1: Identify components

Step 2: Allocate consideration

Step 3: Recognise revenue

### Ind AS 115 Steps

New

Identify the contract(s) with a customer

✓ □

Identify the performance obligations in the contract

New

Determine the transaction price

✓ □

Allocate the transaction price to the performance obligations in the contract

✓ □

Recognize revenue when (or as) the entity satisfies a performance obligation

# Revised Ind AS 115

Current guidance	New standard
Guidance contained in multiple standards and interpretations.	All guidance contained in a single standard
Risk and rewards based model.	Control based model. Risk and rewards is retained as indicator of control transfer for performance obligations satisfied at a point in time.
Revenue is recognised mainly considering the form of the contract.	Revenue is recognised considering the substance of the contract.
No specific guidance on identifying performance obligations in a contract.	Specific guidance on identifying performance obligations in a contract.
Revenue is recognised at the contractual value of the consideration.	Revenue is recognised at the amount of the consideration to which an entity expects to be entitled.

# Revised Ind AS 115

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## Current guidance

Does not provide guidance on combining contracts (except for construction contracts). Currently, revenue is mainly recognised based on the legal form of the contract and at prices stated therein.



No explicit guidance for gross versus net reporting of revenue exists and practice in this area varies.



Limited/no guidance on specific areas like barter, loyalty programmes, costs to obtain a contract, licences etc



Limited disclosure requirements.



## New standard

Explicit guidance on combining of contracts.

The requirement of gross versus net reporting is driven by an assessment of principle versus agent relationship.

Specific guidance on these areas to enable consistency in practice.

Several qualitative and quantitative disclosures required.



# PCM Vs. POCM

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## PCM

- Revenue is recognized only on completion of project
- No consistency on year on year basis
- Impacts the proposed listing as well as existing listings
- Income is recognized on actual basis and not on estimated basis
- Impacts ability to raise funds or avail credit facilities
- Taxation is postponed till completion
- Possibility of loss of brought forward losses
- Impact on deduction under Section 80-IB
- Impact on deduction u/s. 35AD
- Tax Authorities DO NOT appreciate this method and generally litigates

## POCM

- Revenue is recognized on year on year basis based on progress of development
- Income is recognized on estimate basis
- Provides fiscal consistency in the financial statements
- Tax cost is apportioned over different years
- Matches with normal taxation
- Preponed taxation
- Revenue Authorities prefer this method
- Facilitates raising of funds
- Facilitates set off of brought forward losses
- Eligible to avail deduction under Section 80-IB
- Tax Authorities appreciate this method

# Controversies on POCM Vs. PCM

Disputed relating to accounting methods Pre 1 April 2003 – Accounting as per old AS 7

- **Assessee has an option to choose PCM Vs. POCM**
  - Hyundai Heavy Industries Case – 210 CTR 178 (SC)
  - CIT v. Bihalrila Investments – 299 ITR 1 9SC)
- **PCM method approved by the Courts**
  - CIT v. Realest Builders & Services Ltd. – 307 ITR 202 (SC)
  - CIT v. V S Dempo & Co. Ltd. – 131 CTR 203 (SC)
  - Nandi Housing Pvt. Ltd. – 2 SOT 395 (Bang ITAT)
- **PCM Method rejected by the Courts**
  - Champion Construction Co case – 5 ITD 495 (Bom ITAT)
  - Greater Ashoka Land & Dev. Co. Ltd – 79 ITD 595 (Delhi ITAT)
  - CIT v. N M Associates – 256 ITR 141

Disputed relating to accounting methods Post 1 April 2003 – Accounting as per Revised AS 7 and AS 9

- **Assessee has an option to choose PCM Vs. POCM**
  - Awadhesh Builder – 37 SOT 122 – Not a correct ruling
  - Krish Infrastructure Ltd – 35 TM 38 (Jaipur Bench) – Not a correct ruling given the revised AS 7 prescribing only POCM
- **POCM method approved by Courts**
  - CIT v. Manish Buildwell Ltd. – 204 TM 106 (Del)
  - CIT v. SAS Hotel and Enterprises Ltd. – 334 ITR 194 (Mad)
  - Haware Constructions v. ITO – (Mum ITAT)
- **PCM method rejected by Courts**
  - Prestige Estate Projects v. DCIT – 129 ITD 342 (Bang)

# Controversies on POCM Vs. PCM

Income computed as per books of account to be considered in the absence of specific provisions in the IT Act

- ***Specific provisions of the IT Act prevails over the books of account***
- ***In the absence of specific provisions in the IT Act, books of account consistently maintained following AS should be accepted for tax purposes***
  - Challapalli Sugar Mills Ltd. – 98 ITR 167 (SC)
  - CIT v. U P State Development Corporation – 225 ITR 703 (SC)
  - CIT v. Woodward Governor India Pvt. Ltd. – 210 ITR 354 (SC)
  - CIT v. Aatur Holdings Ltd. – 302 ITR 92 (Mum)

Whether Developer can follow PCM method post GN of 2012?

- ***Developer has been consistently following PCM method following AS***
- ***No specific ICDS has been issued thus far by CBDT – Only draft ICDS for real estate developers issued by CBDT***
- ***Guidance Note is not mandatory to be followed by the Developer***
- ***POCM method is not in consonance with IFRS and international accounting practice***
- ***These arguments may not hold good merely on the basis of consistency as it is not in line with the accounting standards and guidelines issued by ICAI Could lead to huge litigations***

# Controversies on POCM Vs. PCM

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Sr no	State	POCM/ PCM?	Case law	Citation
1	<b>Karnataka</b>	PCM	CIT v. Rema Country Holdings Ltd	[2012] 18 taxmann.com 184 (Kar.)
		PCM	Nandi Housing (P.) Ltd. v. DCIT	[2004] 2 SOT 395 (Bang. Trib.)
		PCM	Prestige Estate Projects (P.) Ltd. v. DCIT	[2010] 129 TTJ 680 (Bang. Trib.)
2	<b>Delhi</b>	PCM	Lunar Electricals v. ACIT	[2012] 22 taxmann.com 230 (Delhi HC)
		PCM	CIT v. Manish Build Well (P.) Ltd	[2011] 16 taxmann.com 27 (Delhi HC)
3	<b>Bombay</b>	POCM	Champion Construction Company v. ITO	[1983] 5 ITD 495 (Bom.)
		PCM	Awadhesh Builders v. ITO	[2010] 37 SOT 122 (Mum Trib.)
		PCM	Essar Oil Limited v. DCIT	[2007] 13 SOT 691 (MUM.)
		POCM	Happy Home Developers v. ACIT	[2001] 115 TAXMAN 309(MUM.)(MAG.)

# Valuation of Immovable Property (Section 50C and Section 43CA)

### Section 50C (Applicable for Capital Assets)

- Introduced by Finance Act 2002
- It applies to transfer of immovable property being a Capital Asset.
- The stamp duty valuation shall be considered as full value of consideration for computing capital gains under section 48 if the sale consideration is lower than the stamp duty valuation.

### Section 43CA (Applicable for Stock in Trade)

- Due to inapplicability of Section 50C on immovable property held as stock-in-trade, this section was introduced by Finance Act 2013
- It applies to transfer of immovable property held as stock-in-trade.
- The stamp duty valuation shall be considered as full value of consideration for computing profits and gains if the sale consideration is lower than the stamp duty valuation.

- Where a part or whole of the consideration is received before the date of the agreement for transfer, SDV as on 'date of agreement' rather than the 'date of the registration' may be taken.

- If an assessee claims that the stamp duty value exceeds the fair market value of the property as on the date on the transfer, the AO may refer the valuation of the capital asset to valuation officer.
- Such reference shall be made only if the stamp duty value has not been disputed in any appeal or revision before any authority or Court or the High Court. If any such reference is made, the provisions are Sec. 16A of the Wealth-tax Act shall apply with necessary modification.

- Relaxation granted by Finance Act, 2020 (w.e.f. 1 April 2020) wherein if the stamp duty valuation is higher than 110% of sale consideration, the sale consideration shall be taken as full value of consideration.

# Section 50C & 43CA - Issues

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## **Applicability of sections to rights in land or building**

- Section 50C and 43CA as the case may be applies to land or building or both.
- Land or building v. Rights in land or building
- Favourable decisions-
  - Atul Puranik vs. ITO [2011] 132 ITD 499 (Mumbai),
  - ITO vs. Yasin Moosa Godil 20 taxmann.com 424 Ahm
  - Dy. CIT vs. Tejinder Singh [2012] 50 SOT 391 KOL,
  - Smt Kishore Sharad Gaitonde 2010-TIOL-297-ITAT-MUM,
  - Irfan Abudl Khader 29 taxmann.com 424 (Mum. – Trib.)
  - Kancast Pvt Ltd Vs ITO 2015-TIOL-151-ITAT-PUNE

# Section 50C & 43CA - Issues

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## **Applicability of section 43CA when RE developer applies POCM method**

- Section 43CA is a deeming fiction to substitute sales consideration with SDV for the purpose of computing profits and gains accruing as a result of 'transfer of asset'.
- But, when revenue is recognized on the basis of percentage of completion method, the date of "transfer" of asset is a future event. Also, stamp duty value which would be applicable on the future date of transfer of the asset is not determinable.
- Therefore, whether the deeming fiction of section 43CA can be applied on year to year basis while recognizing revenue based on percentage of completion method?

## **Applicability of section 43CA vs section 44AD**

- Section 44AD overrides only upto section 43C.
- Sections do not mutually override each other.
- Section 44AD refers to 'total turnover' or 'gross receipts'
- Section 43CA provides that the SDV / guidance value shall be the full value consideration



Gift / Transfer of  
Immovable Property  
without adequate  
consideration (Section  
56(2)(x))

# Section 56(2)(x)

56(2)(x)

Income chargeable as 'Other Sources' in the hands of recipient, where property is received at lower than FMV or without consideration

## Issue for consideration

### Key features

- Receipt of **sum of money** or **property** without consideration or for inadequate consideration in excess of Rs. 50,000. **Relaxation of 5% for Immovable Property- w.e.f. AY 2019-20. Relaxation increased to 10% by Finance Act 2020 w.e.f. 1 April 2020;**
- Excess of FMV over consideration to be taxed as Income from other sources;
- **FMV** to be deemed as per **Rule 11UA** – Stamp duty value for immovable property, market value for jewelry, arts, etc., net assets value for other assets.

# Section 56(2)(x)

56(2)(x)

**Income chargeable as 'Other Sources'** in the hands of recipient, where property is received at lower than FMV or without consideration

## Issue for consideration

### Food for thought

- **Double taxation**
  - **First tax u/s 50CA - in the hands of seller**
  - **Second tax u/s 56(2)(x) - in the hands of recipient**
  
- **Cost step-up in the hands of recipient for subsequent sale allowed** – FMV taken as per section 56(2)(x) will be taken as cost of acquisition, in case of subsequent sale by the recipient

# Section 56(2)(x)

56(2)(x)

**Income chargeable as 'Other Sources'** in the hands of recipient, where property is received at lower than FMV or without consideration

## Issue for consideration

- **Whether fresh issue of shares will be covered-**
  - Khoday Distilleries Ltd. v CIT [2009] 307 ITR 312 (SC) – Allotment of shares is appropriation out of unappropriated share capital – Does not amount to **transfer**
  - **Wording of 56(2)(x) is “receives” and not “transfer”**
  
- **Whether issue of Bonus Shares will be covered-**
  - CIT v Dalmia Investment Co. Ltd [1964] 52 ITR 567 (SC) – Bonus shares are without payment but not without consideration

# Section 56(2)(x)

56(2)(x)

**Income chargeable as 'Other Sources'** in the hands of recipient, where property is received at lower than FMV or without consideration

## Issue for consideration

- **Whether issue of Right Shares at less than FMV will be covered-**
  - **Proportionate allotment-** Sudhir Menon HUF v ACIT [2014] 148 ITD 260 (Mum)
  - **Disproportionate allotment-** Sudhir Menon judgement may not apply
- **Whether Buy Back of Shares at less than FMV will be covered-**
  - Vora Financial Services Pvt. Ltd v ACIT [2018] 96 taxmann.com 88 (Mum)- Shares should become “property” of the recipient Company and in that case, it should be shares of any other Company and could not be its own shares. Because own shares cannot become the property of the recipient Company.

# Section 56(2)(x)

56(2)(x)

**Income chargeable as 'Other Sources'** in the hands of recipient, where property is received at lower than FMV or without consideration

## Issue for consideration

### ▪ Issues for valuation under Rule 11UA

- Chain Holding, Multiple Holding, Cross Holding etc.

### Other Issues

#### • Consideration

- ✓ The word 'consideration' is not defined in Sec. 56(2)(x).
- ✓ In the absence of the definition of consideration in Income Tax Act, it must carry the meaning assigned to it in the Indian Contract Act. [*CGT vs. Smt. C.K. Nirmala 215 ITR 156 (Ker – FB) & Chandrakant H.Shah vs. ITO 121 TTJ 145 (Mum)*].

#### • Applicability to Slump Sale at Book Value or lower than FMV?

Income from House Property  
Vs  
Profits and Gains of Business  
or Profession

# IFHP Vs. PGBP

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In the light of various decisions of the SC, the general principles guiding the issue of determination of head under which rental income from property is assessable are laid down in *Universal Plast Ltd. v. CIT (1999) 103 taxman 493 (SC)*. They are:

1. No precise test can be laid down to ascertain whether income (referred to by whatever nomenclature, lease amount, rents, license fee) received by an assessee from leasing or letting out of assets would fall under the head 'Profits and gains of business or profession';
2. It is a mixed question of law and fact and has to be determined from the point of view of a businessman in that business on the facts and in the circumstances of each case, including true interpretation of the agreement under which the assets are let out;
3. Where all the assets of the business are let out, the period for which the assets are let out is a relevant factor to find out whether the intention of the assessee is to go out of business altogether or to come back and restart the same; and
4. If only or a few of the business assets are let out temporarily while the assessee is carrying out his

CBDT in its *circular no. 16/2017 dated 25<sup>th</sup> April 2017*, clarified that the income from letting out of premises/ developed space along with other facilities in an Industrial Park / SEZ is to be treated as business income.



# IFHP Vs. PGBP

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Factors that determine characterization of rental income derived from properties under IFHP or PGBP based on various rulings:

## **Object of assessee**

- The object for which an assessee is formed is of prime importance in deciding as to which side of the line rental income falls.
- If the main object of the assessee is to let out house properties and earn rental income, the rental income is assessable as business income.
- This object, in case of companies, can be ascertained from the Memorandum of Association and Partnership Deed in case of partnership firms / LLPs.

***Chennai Properties & Investments Ltd vs. CIT (2015) 56 taxman.com 456 (SC)***

*Karanpura Development Co. Ltd. v. CIT [1962] 44 ITR 362 (SC)*

*M/s. Rayala Corporation Pvt. Ltd. v. Asst. CIT (2016) 72 taxman.com 149(SC)*

*East India Housing And Land Development Trust v. CIT (1961) 42 ITR 49*

# IFHP Vs. PGBP

## **Intention of the Assessee**

1. The period for which assets are let out is one of the indicators of the intention of the assessee. If the property is let out for temporary period and he intends to come back into the business after the end of lease period, the assets are said to be exploited commercially and the rent is taxable under PGBP.
2. However, if the intention is to earn income merely out of ownership of the asset and rental income is taxable as income from house property or income from other sources, if other assets are also let out and letting is inseparable.

*ITO v. Skipper Properties (P.) Ltd. [2008] 113 ITD 56 (Delhi)*

*CIT v. Vikram Cotton Mills Ltd. [1988] 169 ITR 597(SC) (In this case period of lease was for 19-20 years);*

*Universal Plast Ltd. v. CIT [1999] 103 Taxman 493(SC);*

*Guntur Merchants Cotton Press Co. Ltd. v. CIT [1985] 21 TAXMAN 324 (AP) [Affirmed in Universal Plast Ltd. v. CIT [1999] 103 Taxman 493 (SC)];*

*New Savan Sugar & Gur Refining Co. Ltd. v. CIT (1969) 74 ITR 7 (SC)*

## **Active use of the property**

Whether the property is subject to active use or mere passive possession by the assessee. In the former case, the income is chargeable as business income and in latter, under house property.

*CIT v. Ansal Housing Finance & Leasing Co. Ltd. [2013] 29 taxmann.com 303 (Delhi);*

*Azimganj Estate (P.) Ltd. v. CIT [2012] 20 taxmann.com 203 (Cal.),*

# Taxation of Notional Rental Income [Section 23(5)]

# Section 23(5) - Taxation of Notional Rental Income

Annual Value, in respect of building or land appurtenant thereto, shall be chargeable to tax under 'Income from House Property', which is not rented up to two years\* from the end of the year in which Certificate of Completion is obtained shall be 'NIL' if:

- the building or land appurtenant thereto is held as stock-in-trade, or
- the building or land appurtenant thereto is not let out during the whole of any part of the year.

## Issues :

- Effectively, if stock in trade is unsold for a period of more than 2 years, the same will be subject to notional income tax under the head IFHP
- Constitutional validity of subjecting such notional income to tax;
- Whether the intention of the builder to not let out the property but to only hold the property to sell the same holds any ground if the provision of the act envisages that the property should be in a position to be let out;
- The said section only provides a limited period relief beyond which taxability have to be ascertained as per regular provisions.
- If the annual value can be said to be nil, in a case where property is let out or meant to be let out but the same remains vacant, then there won't be tax liability even beyond one year period specified in the section.

\* Period increased from 1 year to 2 years by Finance Act 2019

# Section 23(5) - Taxation of Notional Rental Income

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## Issues :

- On combined reading of section 23(5) and 71(3A), both introduced by Finance Act, 2017, on one hand, it deems the annual value of house property held as stock-in trade as Nil, if the same is not let out; it appears that the interest deduction would be available under section 24 and consequently, the restriction contained in section 71(3A) would apply to the claim of set off of loss from house property (arising mainly on account of interest deduction) against income from any other head to Rs. 2 Lac.
- This would curtail the benefit of entire interest deduction so far available under section 36(1)(iii).

*SC has granted SLP in the matter of Ansal Housing Finance and Leasing Co. Ltd. wherein the Delhi High Court had ruled ALV of flats lying unsold is assessable as income from house property.*

Conversion of Capital Asset  
into Stock in Trade and *vice  
versa*- Section 45(2) &  
Section 28(via)

# Section 45(2) & 28(via)

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## Section 45(2)

As per section 45(2) if a capital asset is converted into stock-in-trade, the capital gain is taxable in the year such stock is sold, and the fair market value of the asset on the date of such conversion or treatment shall be deemed to be the full value of consideration received or accruing as a result of the transfer.

To bring parity and to discourage the practice of deferment of tax payment on conversion of inventory into capital asset, the Finance Act, 2018 was amended as below:

Section 28(via)/  
2(24)(xiia)

As per section 28(via), the FMV of inventory as on the date of its conversion into, or treated as capital asset shall be chargeable to tax under the head PGBP.

Section 49(9)

Such FMV to be considered as cost of acquisition (COA) for computing capital gains on transfer of converted capital asset.

Section 2(42A)

Period of holding of converted capital asset to be reckoned from the date of conversion thereof.

# Section 45(2) & 28(via)

	Section 45(2)	Section 28(via)
<b>Introduced by F.A.</b>	Finance Act 1984	Finance Act 2018
<b>Head of Income</b>	Capital Gain	PGBP
<b>Point of Taxability</b>	When stock is sold	Mercantile System – In the year of conversion Cash System – in the year consideration is received
<b>Valuation</b>	As on the date of conversion	As on the date of conversion
<b>Valuation Rule</b>	11UA	11UAB

## Issues :

- Clause (via) does not refer to profits arising out of conversion but refers to the Fair Market Value.
- However, it may be pertinent to refer to the provisions of Section 45(2) which provides that the profits or gains arising from the transfer by way of conversion of Capital Asset into or its treatment as Stock-in-trade shall be chargeable to tax as the income of the previous year in which such Stock-in-trade is sold or otherwise transferred.



# Section 45(2) & 28(via)

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## Issues :

- Clause (via) does not refer to profits arising out of conversion but refers to the Fair Market Value. However, it may be pertinent to refer to the provisions of Section 45(2) which provides that the profits or gains arising from the transfer by way of conversion of Capital Asset into or its treatment as Stock-in-trade shall be chargeable to tax as the income of the previous year in which such Stock-in-trade is sold or otherwise transferred.
- The word inventory is not defined under I.T. Act but ICDS – II (Income Computation Disclosure Standards), prescribed u/s. 145 defines the word 'inventory' as 'assets held for sale in the ordinary course of business'. According to Section 28(via), unsold inventory would be treated as the capital asset from the tax point of view as the action of the developer to lease out the unsold premises might be viewed as conversion of inventory into a capital asset.
- In various judicial precedents dealing with matters of conversion of capital asset into stock in trade, it is held that the intention at the time of purchase or acquisition would not be of much relevance. What is of more relevance is to determine the intention at the subsequent point in time, through conduct and affirmative actions, that the capital asset so purchased initially has been converted or treated as stock-in-trade of the business carried on by the assessee.

Recently Delhi ITAT in the case of *M/s. AJB Developers Pvt.* has held that where land was stock in trade in the books of account, but, there was a complete bar on assessee as per the Notification of the Ministry of Defence to raise any construction or to do any business activity therein, the land in question could not be treated as stock in trade but as a capital asset in nature determining holding period from the date of acquisition.

# Joint Development Arrangements

# Joint Development Mechanism

Upfront consideration



Enters into development agreement

% share in revenue

% share in revenue

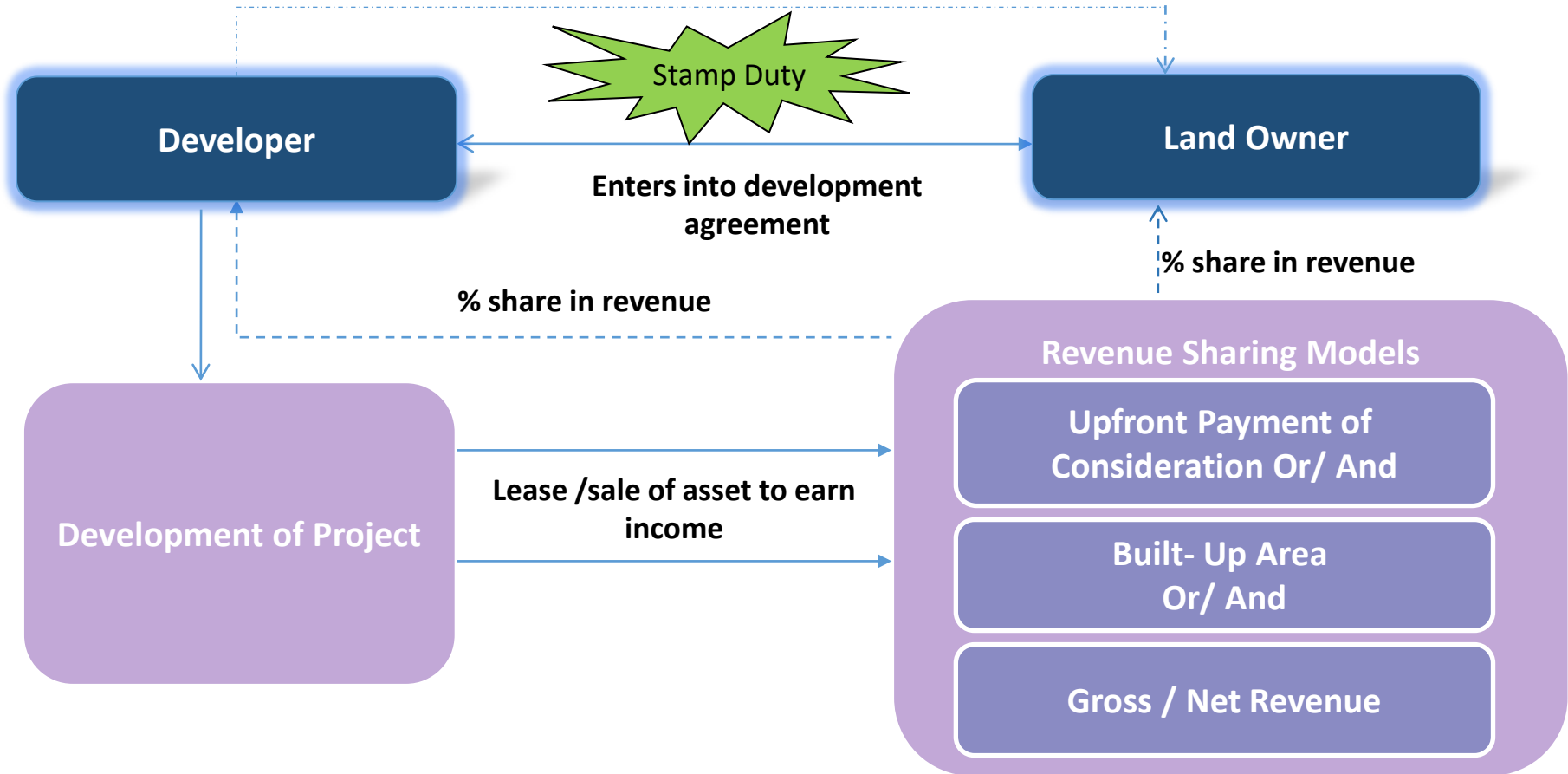
Lease /sale of asset to earn income

Revenue Sharing Models

Upfront Payment of Consideration Or/ And

Built- Up Area Or/ And

Gross / Net Revenue



# Nature of Asset

Taxability on entering into JDA will depend upon the nature of asset held by the land owner ...

## Business Income

- Accounting Policy - Revised Guidance Note 2012 vs. Ind AS 115
- Conveyance Theory vs. Possession Theory
- Impact of Section 2(47)(v) and section 43CA of the Act
- Legal Implications – TOPA
- Accounting Policy vs. Accrual Income Theory (as per tax laws)



## Capital Gains

- Section 45 – Chargeable in the year of transfer of capital asset
- Point of Taxability – Section 2(47)(v) of the Act read with section 53A of the TOPA
- Transfer of Possession and satisfaction of other conditions

## Capital Gains and Business Income

- Section 45(2) - Taxable in the year of sale or transfer of the stock in trade
- Capital Gains – FMV (-) COA
- Business Income – Sale consideration (-) FMV

# Tax Controversies- JDA

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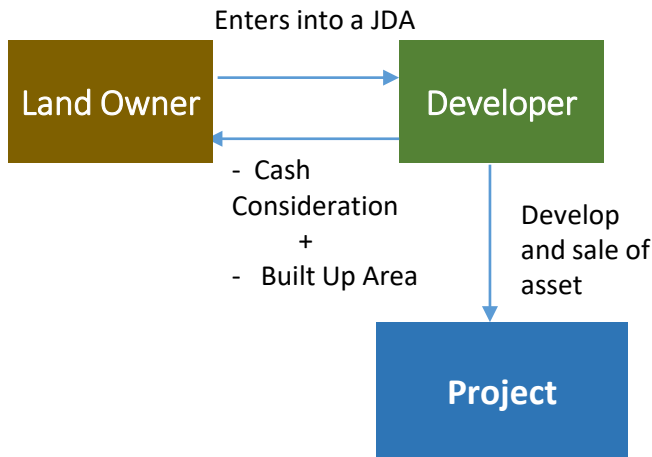
## Taxability of Income in the case of JDA

- *Taxability in the hands of land owning company – asset held as capital asset of stock in trade*
- *Area Sharing vs Revenue Sharing arrangements*
- *Deductibility of various payment by the Developer to land owner*
- *AOP issues*
- *Stamp Duty and GST issues*

# Taxability under JDA in the hands of Land Owner

Entering into JDA will trigger either business income or capital gain liability depending upon whether the immovable property has been held as stock-in-trade or capital asset.

## Stock-in-Trade



## Joint Development Agreement – Point of Taxability

### Facts of Case

- Land owner enters into a Joint Development Agreement with the developer to develop the property
- Land owner gives possession of land coupled with general power of attorney
- General Power of Attorney in favour of developer granting rights to obtain license from government authorities, carry the construction work, carry out the advertising activities, collection of advance from the proposed buyers, etc.

**Issue:** When the business income accrues or arises?

- At the time of entering into development agreement and execution of General Power of Attorney; or
- At the time of execution of conveyance deed in favour of ultimate buyer; or
- At the time of receipt of Built up area from Developer; or
- At the time of sale of Built up area in favour of third party purchaser?

# Capital Gains Taxability in the hands of Land Owner- Individuals and HUF

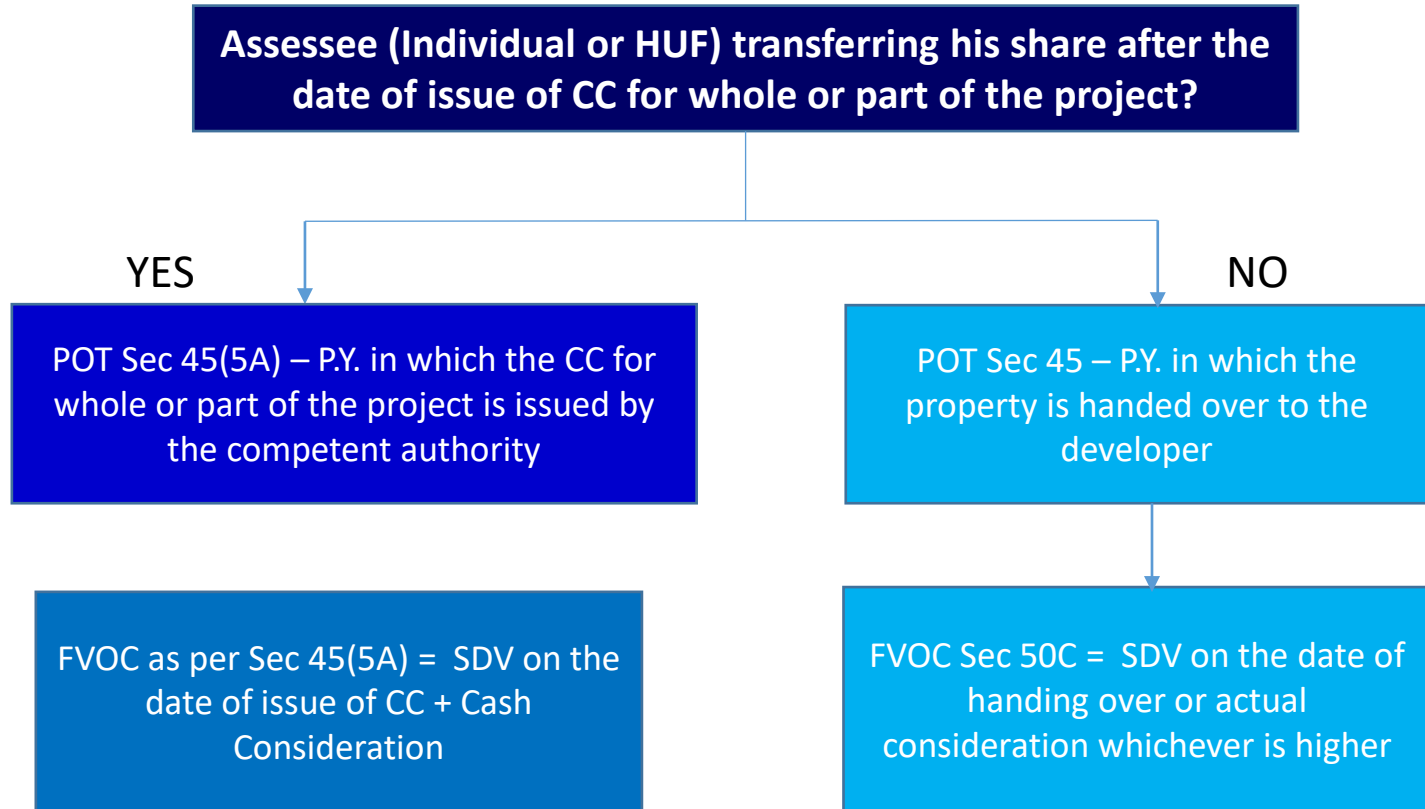
## Amendment by Finance Act, 2017- Relief granted to Individuals and HUFs

### Section 45(5A)

- ***Capital Gain arising to an individual or a Hindu undivided family, from the transfer of a capital asset, being land or building or both, under a specified agreement***
- ***Capital Gains shall be chargeable to income-tax as income of the previous year in which the certificate of completion for the whole or part of the project is issued by the competent authority;***
- ***Stamp Duty Value, on the date of issue of the said certificate, as increased by the consideration received in cash, if any, shall be deemed to be the Full Value of Consideration received or accruing as a result of the transfer of the capital***

- *Section 45(5A) shall not apply where the assessee transfers his share in the project on or before the date of issue of the certificate of completion*
- *Capital Gains shall be deemed to be the income of the previous year in which such transfer takes place*
- *Normal Provisions shall apply for the purpose of determination of full value of consideration*

# Capital Gains Taxability in the hands of Land Owner- Individuals and HUF



If any developer pays any amount to the land owner in addition to the share in the project, then such developer shall deduct TDS @10% under section 194-IC, overriding the provision of section 194-IA.



# Section 45(5A)- Issues

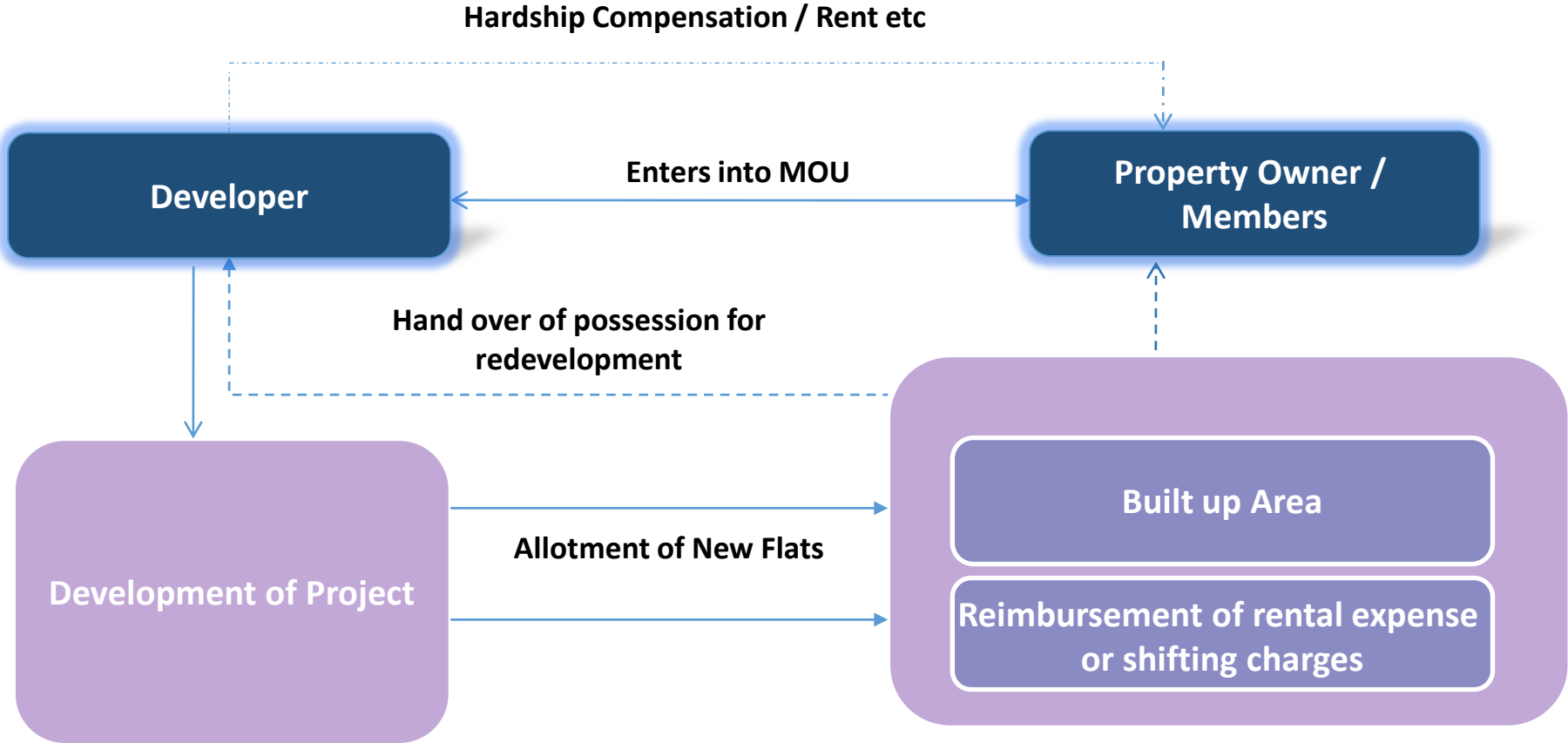
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## **Issues pertaining to section 45(5A):**

- There still remains the difference in timing between the POT and receipt of consideration under JDA.
- Why the benefit is restricted only to Individual and HUF?
- Whether the benefit of indexation on cost/improvement would be also available till the receipt of CC?
- The time limit for claiming the benefit under 54 & 54F should also be extended from the date of issue of CC and not from the date of transfer.
- Reference to Valuation officer should also be extended to the provision of section 45(5A)

# Redevelopment Projects & Slum Redevelopment Projects

# Redevelopment Projects- Mechanism



# Tax Treatment in Redevelopment / SRA Projects

## **Taxability in the hands of Property Owner (Individuals):**

- Surrender of immovable property is transfer under Section 2(47) of the Act against right to possess a new flat in future.
  - Date of Transfer – Date of certificate of completion for redeveloped property
  - Sale Consideration- Stamp Duty Value on the date of transfer plus cash compensation
  - Claim exemption under Section 54 – In effect no capital gain payable
- Reimbursement of expense is not income. Hence, not taxable.
- Hardship Compensation is not taxable being capital receipt. [*Jethalal D Mehta v Dy CIT (2005) 2 SOT 422*]
- In case the owner transfers his rights under the agreement before completion of the project, then, the year in which he so transfers his rights shall be deemed to be the year of transfer of the rights in property and capital gains computations and holding period computations, shall be done accordingly.
- Whenever the new property is transferred in future, the stamp duty value taken as consideration, shall be treated as the actual cost to him for capital gains computations.

## **Tax Deducted at Source by developers:**

The developer shall deduct TDS @10% of cash consideration with no threshold limit.

# Tax Treatment in Redevelopment/ SRA Projects

## Taxability for Builder/Developer:

- Compensation paid to tenants/lessee can be reduced from full value of consideration: *CIT v A. Venkataraman and Others (1982) 137 ITR 846 (Mad.)*
- Undertaking developing and building Housing Project – Eligible for 80-IBA even if developer not owner of land. [*Radhe Developers & Ors. vs. ITO & Ors. (2008) 23 SOT 420 (Ahd.)*]
- Where construction project has long gestation period and percentage completion method is adopted for income-tax purpose, losses only proportionate to work completed during year can be allowed and not entire anticipated loss :
  - *Shivshahi Punarvasan Prakash Ltd. v. ITO-10(1)(4) (2011) 15 taxmann.com 352 (Mum Trib.)*
- Where assessee claimed deduction of slum development expenditure which was contingent upon authority giving vacant possession of plot, in view of fact that authority was unable to hand over vacant possession of land, impugned claim was to be disallowed :
  - *Grace Shelter v. ACIT [2019] 104 taxmann.com 133 (Mum)*
- Where assessee-builder entered into contract for development of SRA project (Slum rehabilitation), since assessee had to pay certain compensation to slum developers due to its failure to provide alternative accommodation during period of construction, said payment not being in nature of 'rent', did not require deduction of tax at source under section 194-I:
  - *Sahana Dwellers (P.) Ltd. v. ITO [2016] 67 taxmann.com 202 (Mum Trib.)*

# Tax Treatment in Redevelopment Projects

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## **Taxability for Tenants :**

- Surrender of tenancy Rights – Transfer u/s. 2(47) – Cost of acquisition: *Balmukund P. Acharya vs. ITO (2011) 48 SOT 385 (Mum)*
- Capital gain – Sale proceeds of tenancy rights exemption u/s. 54EC : *ACIT vs. Vijay S. Shirodkar (2011) 48 SOT 8 (Mum)*

# Tax Treatment in Slum Rehabilitation Projects

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## **Slum Rehabilitation Project:**

- Section 35AD provides for a deduction of the profits of an undertaking developing and building housing project.
- One of the condition is that the Slum Rehabilitation scheme has to be notified by the Board.
- These SRA projects has to be in strict compliance of various rules and Act, which is again guided by the Circulars and Notifications, therefore, the developer has no say in its implementation and execution.

# Budget Proposals 2021-22



# Key Announcements for the Real Estate Sector

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- In the previous budget, the government provided an additional deduction of interest, amounting to INR 1.5 lakh, for loan taken to purchase an affordable house. The deduction has been extended by one more year until 31 March 2022.
- To keep up the supply of affordable houses, it is proposed that affordable housing projects can continue to avail a tax holiday for one more year until 31 March 2022 . Further, to promote supply of affordable rental housing for migrant workers, the FM has proposed to expand the scope of tax holiday/ deduction to cover notified rental housing projects until 31 March 2022.
- For applying provisions of deemed taxation, the safe harbor limit in form of variation between the transaction value and the stamp duty value of land or building or both, increased to 20 per cent from the erstwhile limit of 10 per cent for transfer of residential units during the period 12 November 2020 to 30 June 2021, subject to specified conditions.
- Sovereign Wealth Funds ('SWF') and Pension Funds ('PF') will now be permitted to make investment into Category I and Category II AIFs which in turn are permitted to make investment in InvITs ;. Also, it is proposed to relax the condition of 100% to 50% for investment in eligible infrastructure companies. Further, SWF/PF are now also allowed to invest through holding company subject to fulfilment of specified conditions.

# Key Announcements for the Real Estate Sector

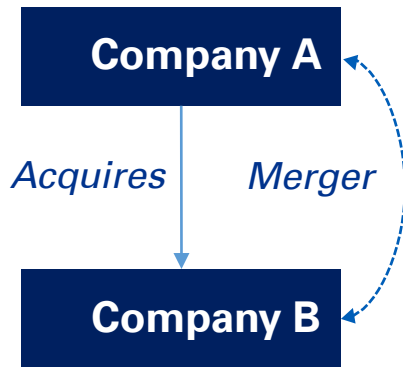
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- The time limit for providing exemption of capital gain which arises from the transfer of a residential property, owned by the eligible assessee is proposed to be extended from existing 31 March 2021 to 31 March 2022 if the net consideration is utilised for subscription of equity shares of an eligible start-up. Similarly, outer date for incorporation of eligible start-up is also proposed to be extended to 31 March 2022 from 31 March 2021.
- Tax audit threshold further increased to INR 10 crore from existing INR 5 crore, subject to certain conditions.
- Rationalization of equalization levy provisions to bring more transactions under the purview
- Due date for filing of Belated Return and Revised Return has been now been further reduced by three months. Effectively, the belated return or revised return could now be filed three months before the end of the relevant assessment year or before the completion of the assessment, whichever is earlier.
- Late deposit of Employee Contribution by the Employer to the relevant fund will be disallowed as deduction in the hands of the employer.

# Depreciation on Goodwill of Business or Profession

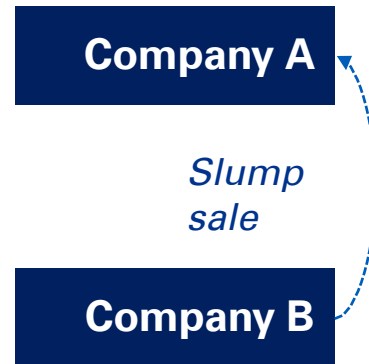
## Illustrative structure resulting in Goodwill

### A. Share acquisition & merger



- **Company A acquires Company B**
- **Post acquisition, Company A and Company B are merged**
- **Goodwill is recorded on such merger**

### B. Purchase of business



- **Company A acquires business from Company B for cash consideration**
- **Goodwill is recorded on account of purchase price allocation**

## Proposed amendments\*

*Goodwill of business or profession derecognized as a depreciable asset*

*For acquired goodwill, cost to remain available for capital gains purposes (depreciation claimed until FY19-20 to be reduced from purchase price)*

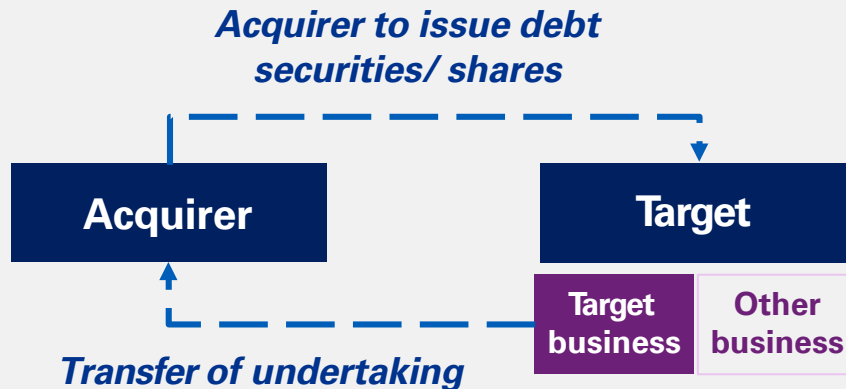
*Rules to be provided for calculation of WDV and short-term capital gains (if any) where WDV in FY19-20 includes goodwill*

### Open points

- *Prospective amendment – however, depreciation claimed earlier may still be questioned on technical aspects?*
- *Recognition of other intangibles on merger/ acquisition – possible to claim depreciation?*

\*Amendment effective from FY starting April 1, 2020

# Slump Sale to include exchange



## At present

Current definition of 'slump sale' is restricted to transfer of undertaking as a result of sale

Some judicial precedents have distinguished 'slump exchange' from 'slump sale'

## Proposed amendment

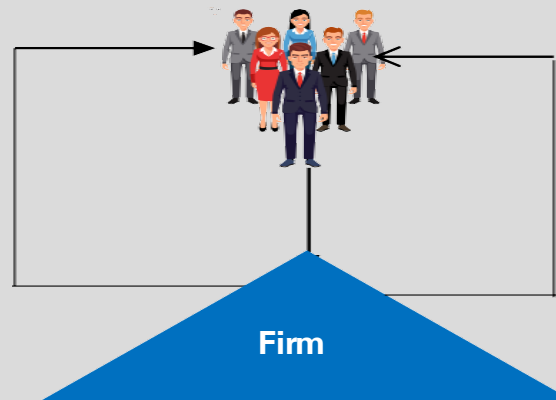
- Definition of 'slump sale' to be expanded to include transfer of undertaking by any means (i.e. exchange also to be included)
- Reference given to the definition of "transfer" u/s. 2(47)
- Amendment effective from FY starting April 1, 2020

# Dissolution or Reconstitution of Firm

## A. If receipt of capital asset represents capital account balance in firm books

### Existing

- Consideration = FMV of capital asset



### Proposed\*

- Consideration = FMV of capital asset
- Cost of acquisition = Cost of capital asset
- Capital account excludes effect of revaluation or self generated goodwill/asset

\*Amendment effective from FY starting April 1, 2020

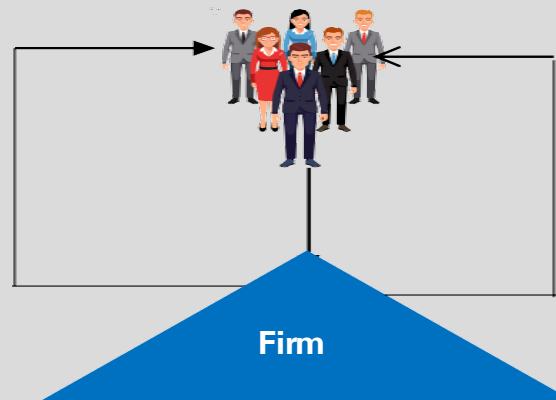
Key Impact: Proposed amendment intends to address the tax avoidance structures (through revaluation of assets in the partnership firm and distribution of restated capital balance to partners)

# Dissolution or Reconstitution of Firm

## B. If receipt of money/ asset in excess of capital account balance in firm books

### Existing

- No specific provision
- Distribution of restated capital pursuant to revaluation assets – tax treatment is matter of judicial debate



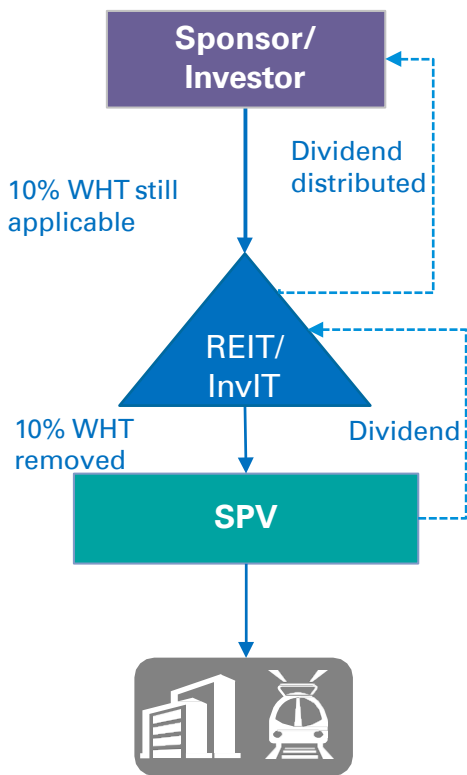
### Proposed\*

- Consideration = Value of money + FMV of asset
- Cost of acquisition = Capital account balance
- Capital account explicitly excludes effect of revaluation or self generated goodwill/ asset
- On subsequent sale of Capital Asset, revalued amount taxed u/s 45(4A) to be reduced from consideration
- No access to treaty even if partner is a NR

\*Amendment effective from FY starting April 1, 2020

Key Impact: Proposed amendment intends to address the tax avoidance structures (through revaluation of assets in the partnership firm and distribution of restated capital balance to partners)

# REIT / InvIT: Withholding tax on Dividend Income



Where Hold Co and SPV opt for 22% tax rate

## Current Law

- ✓ Exempt if SPV under old tax regime
- ✓ R – taxable at applicable rates
- ✓ NR – 20%

- ✓ Exempt
- ✓ WHT @ 10% on dividends distributed if taxable

- ✓ WHT @ 10% - Old

Cash Trap at REIT / InvIT Level

Where Hold Co and SPV opt for 22% tax rate

## Budget 2021 Proposed

- ✓ Exempt if SPV under old tax regime
- ✓ R – taxable at applicable rates
- ✓ NR – 20%

- ✓ Exempt
- ✓ WHT @ 10% on dividends distributed if taxable

- ✓ WHT @ 0%

Cash Trap Removed

- Debt Financing of InvITs and REITs by Foreign Portfolio Investors to be enabled
- NHA and Powergrid to set up InvITs

# Faceless Scheme for ITAT Proceedings [S. 255 (7), (8) & (9)]

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- Faceless scheme for ITAT proceedings to be launched before 1 April 2023 on the same line as faceless appeal scheme
  - To reduce human interface from the system, reduce cost of compliance for taxpayers, increase transparency, work distribution in different Benches resulting in best utilization of resources
- The Scheme will take effect from 1 April 2021
- FM Speech-
  - National Faceless ITAT Centre to be established
  - All communication between ITAT and taxpayer shall be electronic
  - Personal hearing (if needed) shall be conducted through VC

## ***Issue***

- No clarity on the impact on 'personal hearing'?



# Income-tax Settlement Commission (ITSC) discontinued

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- ITSC to be discontinued from 1 February 2021 [S. 245C]
- Government to constitute one or more Interim Board (IB) for settlement of pending cases [S. 245AA]
- Every Interim Board shall consist of three members of the rank of Chief Commissioner
- Option to withdraw pending application within 3 months from the date of commencement of the FA, 2021 [S. 245M]
- Income-tax authority shall not be entitled to use the material produced before ITSC except it has been collected / recorded during other proceedings
- Faceless scheme to be introduced (before 31 March 2023) for proceedings before IB

## ***Issues***

- No alternative for ITSC has been provided
- New 'Dispute Resolution Committee' (DRC) is not an alternative -
  - It is only for small taxpayers and it will not cover large cases
  - Search and seizure cases have been kept out of the purview of DRC

# Dispute Resolution Committee (DRC) [S. 245MA]

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- In order to provide early tax certainty to small and medium taxpayers, DRC will be constituted
  - The aim is to prevent new disputes and settle issues at the initial stage
- DRC to resolve disputes of specified persons or class of person – to be notified
- Taxpayers will have an option to opt for or not to opt for dispute resolution through DRC
- Only disputes where the returned income is  $\leq$  INR 5 million and the aggregate amount of variation proposed in assessment is  $\leq$  INR 1 million shall be eligible to be considered by DRC
- Specified orders shall not be eligible for DRC if the order is based on search or survey or on an information received under an agreement u/s. 90 or 90A
- Taxpayer would not be eligible for this benefit if there is detention, prosecution or conviction under specified laws
- DRC to have powers to reduce or waive any penalty or grant immunity from prosecution
- E-resolution scheme to be notified before 31 March 2023

# New procedure of Reassessment, Search & Survey assessment

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- AO may reassess any income which has escaped assessment as against earlier where the AO required 'reason to believe' that income has escaped assessment – [S. 147]
- AO to serve a notice requiring taxpayer to furnish return of income if there is 'information' suggesting that income has escaped assessment – [S. 148]
  - Any information flagged as per the risk management strategy formulated by CBDT (flagging to be done by the computer-based system)
  - Final objection raised by CAG that assessment is not as per the provisions of the Act
- New procedure for re-assessment for cases of income escaping assessment including search cases, to reduce litigation and provide ease of doing business – [S. 148A]
  - AO to conduct enquiries and provide an opportunity of being heard to taxpayers before issuing reopening notice
  - No opportunity to be given in search/requisition cases
  - Prior approval of specified authority is also required to be obtained before issuance of notice
  - Basis the reply, AO to decide whether to issue a notice within one month from the receipt of reply or within one month from the end of the extended time period

# New procedure of Reassessment, Search & Survey assessment

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- Time-limit for re-opening of assessment reduced from 4/6 years to 3 years from the end of relevant AY (reopening with prior approval of PCIT) – [S. 149]
  - Only in specific cases where income escaping assessment (represented in the form of an asset) exceeds / likely to exceed INR 50 lakh or more, time-limit of 3 years stands enhanced to 10 years (with prior approval of PCCIT)

## **Search and seizure cases**

- Assessment / re-assessment / income re-computation for search cases u/s 132 / requisition u/s 132A conducted on or after 1 April 2021 to be included under the new procedure [S. 147, 148A, 153A]
  - Substituted S. 148 provides for deeming provision that income has escaped assessment where search and seizure has taken place
  - Assessment to be made of the previous 3 or 10 AYs as the case may be

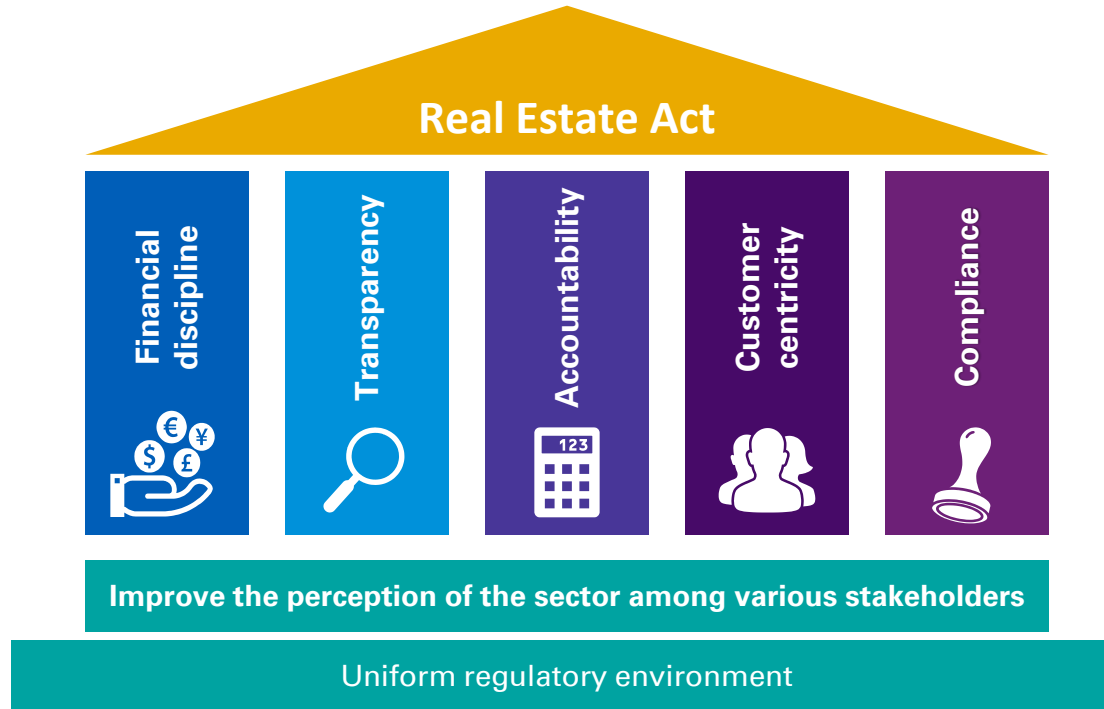
# New procedure of Reassessment, etc- Issues

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- Phrase 'reason to believe' has been removed
  - 'Reason to believe' words are stronger, and the belief entertained by AO must not be arbitrary or irrational – *Raymond Woollen Mills Ltd. (236 ITR 34)*, *Ganga Saran & Sons (P.) Ltd. (130 ITR 30)*, *Nawab Mir Barkat Ali Khan Bahadur (97 ITR 239) (SC)*
- Mere 'change of opinion' (having 2<sup>nd</sup> thought on the same material, etc.) cannot form the basis for reassessment – *Bhanji Lavji (79 ITR 582)*, *Nawab Mir Barkat Ali Khan Bahadur (97 ITR 239) (SC)*
  - Whether this concept is still relevant under the new regime?
- Supreme Court decision overruled-
  - CAG report cannot be considered as 'information' under (the erstwhile) Section 147(b). The AO must have reason to believe that income has escaped to reopen the case. The opinion rendered by the audit party in regard to the law cannot, for the purpose of such belief, add to or colour the significance of such law - *Indian & Eastern Newspaper Society 119 ITR 996 (SC)*
- Empowers AO to reopen cases under the Survey without giving opportunity of hearing

# RERA and its Implications

# Overview of RERA- Pivotal Pillars of the Act



**COMMERCIAL** and **RESIDENTIAL** projects including **PLOTTED DEVELOPMENT**

Land under development **MORE THAN 500 SQ MTS / NO. of UNITS** exceed **8**

Projects which do not have **COMPLETION CERTIFICATE** before commencement of **ACT**

**RENOVATION** or **REPAIR** or **REDEVELOPMENT** projects not involving Marketing, Advertising, Selling & New Allotment **NEED NOT BE REGISTERED**

# Tax Impact of RERA

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- Possibility of AOP exposure in the case of JDAs considering that the land owner is also considered to be a promoter
- Reorganising of JDA arrangement, especially the revenue share arrangement
- Tax treatment / allowability of expenditure done by a promoter during defect liability period
- Tax treatment / allowability of fines, penalties and interest paid by the promoter
- Treatment of expensed incurred on a project which is then taken over by the Authority in the case of lapse in registration or revocation of registration



# Any Questions?

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**Questions**

**&**



**Answers**

THANK YOU!

CA VYOMESH

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