GST शास्त्र – All about TDR transactions under construction sector

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> **History & introduction of the concept:**

The instrument of TDR is considered as a tool to control urban sprawl and achieving development of cities to large extent. As per the literatures available, the concept of TDR was 1st introduced in United States in 1968 as a development control measure.

Central Govxernment, State Government or Local Authorities are required to provide certain civic facilities or amenities to citizens. Road widening, parks, playgrounds or schools are some of the amenities which, the concerned Government, are required to provide and hence they are required to acquire land for the development purpose. Such acquisition of land used to be done through Land Acquisition Act. Against acquisition of land, concerned Government used to pay monetary consideration which involves huge cash outflow. Such procedures took prolonged time and in various cases led to litigations between landowners and Government. In order to overcome these issues, Government came out with a concept of providing consideration to landowners in the form of **"Transferable Development Rights"** which makes available certain amount of additional built up area **(additional FSI)** in lieu of land area relinquished.

Further, a land has various rights attached to it. Some of the rights are right to occupy, right to let out, right to lease, right to easement, right to sale, right to mortgage etc. **Right to develop** land is also one of the rights attached to land. In common parlance, right to develop is a right which enables or permits a person to develop a structure on land.

TDR vs TDR

It is important to note that there is difference between ***"Transferable Development Rights"*** and ***"Transfer of Development Rights"***. The acronym ***TDR*** is generally used for both in common parlance. Transferable Development Rights are in the form of certificates, commonly known as **"Development Rights Certificate (DRC)"** which may be used by owner of the land himself or it may be transferred to any other person for a consideration. The owner of such certificate is entitled to load the **extra built up area (additional FSI)** over any other land owned by DRC holder. However, Development Rights enables transferee to develop land to which such rights are attached and not any other land.

> **Applicability of GST on transfer of TDR:**

Among the all the ambiguities after introduction of GST, the legislative intention is to tax transactions in TDR, may it be transfer of development rights or transferable development rights. For detailed discussion on taxation under erstwhile laws, judicial pronouncements, readers may refer previous article ***"GST शास्त्र – Mystery of applicability of GST on Transferable Development Rights (TDR)***.

Author restricts this article to the discussion on applicability of GST on such transactions and intends to discuss various eventualities under construction sector where such transactions take place.

> Tax implications under joint development agreements (JVs):

In such type of arrangements, the landowner enters into agreement with developer, whereby, the landowner **transfers development rights** to construct or develop a complex to the developer. In return, developer agrees to assign either a portion of the constructed area, which is commonly known as area sharing agreement, or agrees to share revenue realized out of the sale of constructed area, which is commonly known as revenue sharing agreement. Further, in such kind of arrangements, developers are also entitled to FSI or additional FSI derived out of the land parcel.

Let's analyze above 2 models in details and GST implications on transfer of development rights.

√ **Area sharing agreements :**

In such kind of arrangement, the consideration against transfer of development rights is in the form of construction service.

a) Rate of Tax –

In the absence of any specific entry of concessional rate, such activity is taxable **@18%.** However, it is **subject to ceiling of 1% or 5%** in case of affordable and non-affordable **residential apartments (including commercial units in RREP*)** respectively, as prescribed under valuation part below.

*(*RREP – mean a Real Estate Project in which the carpet area of the commercial apartments is not more than 15 per cent. of the total carpet area of all the apartments in the Real Estate Project.)*

b) Exemption –

As per **notification no. 4/2019 – Central Tax (Rate) dt. 29th March, 2019**, exemption has been provided to service by way of development rights on or after 1st April, 2019 for construction of **residential apartments** by landowner.

However, such exemption is subject to sale of flats before date of issuance of completion certificate or first occupation of project whichever is earlier.

It implies that GST is payable in proportion to area of flats remained unbooked as on date of issuance of completion certificate or first occupation of project whichever is earlier. Also, exemption is granted to above mentioned service for construction of residential apartments and not for the construction of commercial apartments.

c) Valuation –

Valuation mechanism has been provided in **notification no. 4/2019 – Central Tax (Rate) dt. 29th March, 2019**.

There could be monetary as well as non-monetary consideration involved in the transaction. Tax impact on the same shall be as follows :

(I) Monetary consideration :

Final liability to be calculated on the monetary consideration paid against development rights in the ratio of un-booked residential units as on the date of completion certificate or first occupation of project whichever is earlier.

Formula : Monetary consideration (x) Carpet area of residential flats remain unsold (÷) Total carpet area of project.

(II) Non-monetary consideration : Units given to landowners value shall be calculated according to paragraph 1A as mentioned below. However, such value shall not exceed 1% of the value in case of affordable residential apartments and 5% of the value of non-affordable residential apartments. Value of apartments remained un-booked is to be calculated according to paragraph 1B.

Paragraph 1A :

Value of supply of service by way of transfer of development rights or FSI by a person to the promoter against consideration in the form of residential or commercial apartments shall be **deemed to be equal to the value of similar apartments** charged by the promoter from the independent buyers **nearest to the date on which such development rights or FSI is transferred** to the promoter.

Paragraph 1B :

Value of portion of residential or commercial apartments remaining un-booked on the date of issuance of completion certificate or first occupation, as the case may be, shall be deemed to be equal to the value of similar apartments charged by the promoter nearest to the date of issuance of completion certificate or first occupation, as the case may be.

Thus, valuation mechanism of service by way of transfer of development rights has two fold effects.

1. Calculate value on the date of transfer of development rights for entire area of project considering value charged for similar apartment from independent buyer nearest to the date on which such development rights are transferred.

The value calculated as per above mechanism pertains to complete area of the project including area of residential flats remain unsold. Hence, in case of residential apartments, proportionate tax payable on value of flats remained unbooked is to be calculated as follows –

Value as calculated above (x) Carpet area of residential flats remain unsold (÷) Total Carpet area of project.

As there is no exemption to service provided by way transfer of development rights for construction of commercial apartments, there is no need to calculate proportionate value for un-booked commercial apartments.

2. In case of residential apartments, tax payable calculated @ 18% on value calculated as above, shall not exceed 1% of value of similar affordable and 5% of value of similar non-affordable apartments charged by the promoter nearest to the date of issuance of completion certificate or first occupation, whichever is earlier.

Thus, tax payable on value of flats remained un-booked is to be calculated as follows –

Value of un-booked affordable residential flats (x) 1% (+) value of un-booked non affordable residential flat (x) 5%

Value is to be considered nearest to the date of issuance of completion certificate or first occupation, whichever is earlier.

Final tax liability on service by way of transfer of development rights for construction of **residential apartments** shall be lower of tax calculated as per step 1 and step 2.

In case of commercial apartments, final tax liability shall be calculated **@18%** on value as prescribed in paragraph 1A only. Though valuation mechanism under paragraph 1B is provided for residential and commercial apartments, in the opinion of author, only mechanism of paragraph 1A is applicable to commercial apartments. It is because there is no exemption in respect of development rights transferred for construction of commercial apartments and condition as mentioned against serial no. 41A of the notification, specifically talks about valuation of un-booked **residential apartments** as on the date of completion certificate or first occupation in project, whichever is earlier.

d) Reverse charge mechanism –

As specified in **notification no. 5/2019 – Central Tax (Rate) dated 29th March, 2019**, where service is supplied by way of transfer of development rights for construction of **residential as well as commercial apartments**, tax is to be paid by recipient as specified in section 9(3) of **CGST Act, 2017**. Hence, developer, who is recipient, shall pay tax on service specified above.

e) Time of supply –

As per entry (i) read with entry (a) of **notification no. 6/2019 – Central Tax (Rate) dated 29th March, 2019**, where against supply of development rights, consideration is paid in the form of **residential as well as commercial apartments,** time of supply shall arise on the date of issuance of completion certificate for the project or on its first occupation, whichever is earlier.

Further, as per entry (i) read with entry (b) of the same notification, where against supply of development rights relatable to construction of **residential apartment**, monetary consideration is paid, time of supply shall arise on the date of issuance of completion certificate for the project or on its first occupation, whichever is earlier. However, it implies that where such development rights are relatable to commercial apartments and where monetary consideration is paid, time of supply is not deferred.

All the above provisions are *mutatis mutandis* applicable to transactions in transferable development rights.

√ **Revenue sharing agreements :**

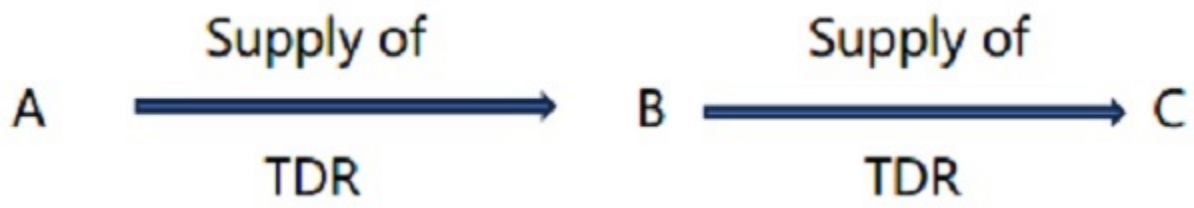
In this kind of arrangement, consideration against transfer of development rights is in the form of revenue derived out of sale of constructed units. Landowner sources development rights and developer sources expertise and capital. Whatever profits! losses of business are shared between these two parties. Hence, such kind of arrangements are akin to partnership wherein both the partners introduce capital in agreed ratio and enjoys profit! loss earned out of business.

Hence, in the opinion of author, introduction of development rights in these kinds of arrangements do not qualify as supply and hence not liable to tax under GST to the extent of consideration in the form of revenue shared out of sale of constructed units.

> **Tax implications on trading of transferable development rights:**

Considering profit opportunities, some of the taxpayers, instead of utilizing additional FSI by holding Development Rights Certificates, sale to other persons and enjoys profit. However, taxability in the hands of supplier or recipient of service depends upon its utilization which is discussed below.

Let's discuss the scenario with the help of illustration.



(i) Taxability in the hands of Mr B at the time of procurement of DRC certificate –

W.e.f 1st April, 2019, reverse charge u/s 9(3) of CGST Act, 2017, on supply of services by way of transfer of development rights or FSI or additional FSI was introduced. As per the **notification no. 5/2019 – CT (R) dt. 29th March, 2019**, tax on services supplied by any person by way of transfer of Development rights or FSI including additional FSI for construction of a project by a promoter is to be paid by promoter on reverse charge basis.

It is pertinent to note that reverse charge is applicable on such transaction only where additional FSI is used for construction of a project by a promoter. In this scenario, Mr. B has not consumed additional FSI but further sold DRC certificate to other parties.

Hence, in this case, reverse charge liability shall not arise in the hands of recipients i.e Mr. B. Infact, such liability shall arise in the hands of suppliers of DRC certificates i.e Mr. A on forward charge basis, since liability u/s 9(3) of CGST Act, 2017 was not shifted to the recipient where FSI has not been used for construction of a project by a promoter.

(ii) Taxability in the hands of Mr B at the time of sale of DRC certificate –

As discussed above, shifting of tax liability u/s 9(3) of CGST Act, 2017, depends on end use of the FSI or additional FSI.

If after sale of TDR by Mr. B, Mr. C has consumed or willing to consume the FSI or additional FSI for construction of a project, liability will get shifted to such promoter by virtue of **notification no. 5/2019 – CT (R) dt. 29th March, 2019**.

However, if even after sale of TDR by Mr. B, recipient Mr. C has further sold it to any other party, in the opinion of author, liability shall arise in the hands of Mr. B.

Hence, this scenario, facts of the case and agreement between parties in relation to use of DRC certificate will play vital role in determination of taxability.

> **Conclusion :**

Considering above scenarios, taxability in case of transfer of development rights or transaction of DRC certificates is to be analysed in advance. Especially, in the state of Maharashtra, GST department is obtaining data from municipal corporation and all the transactions are under scanner.

(Above article was written on 18th November, 2023 & jointly authored by CA. Yogesh Ingale, CA. Tushar Ajmera and CMA Anuj Chordiya. Views expressed are strictly personal. For any queries & feedback, reach us at yogesh.ingale@talentax.in).

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