GST शास्त्र-Redevelopment agreements – Taxability & other aspects (Part 1)

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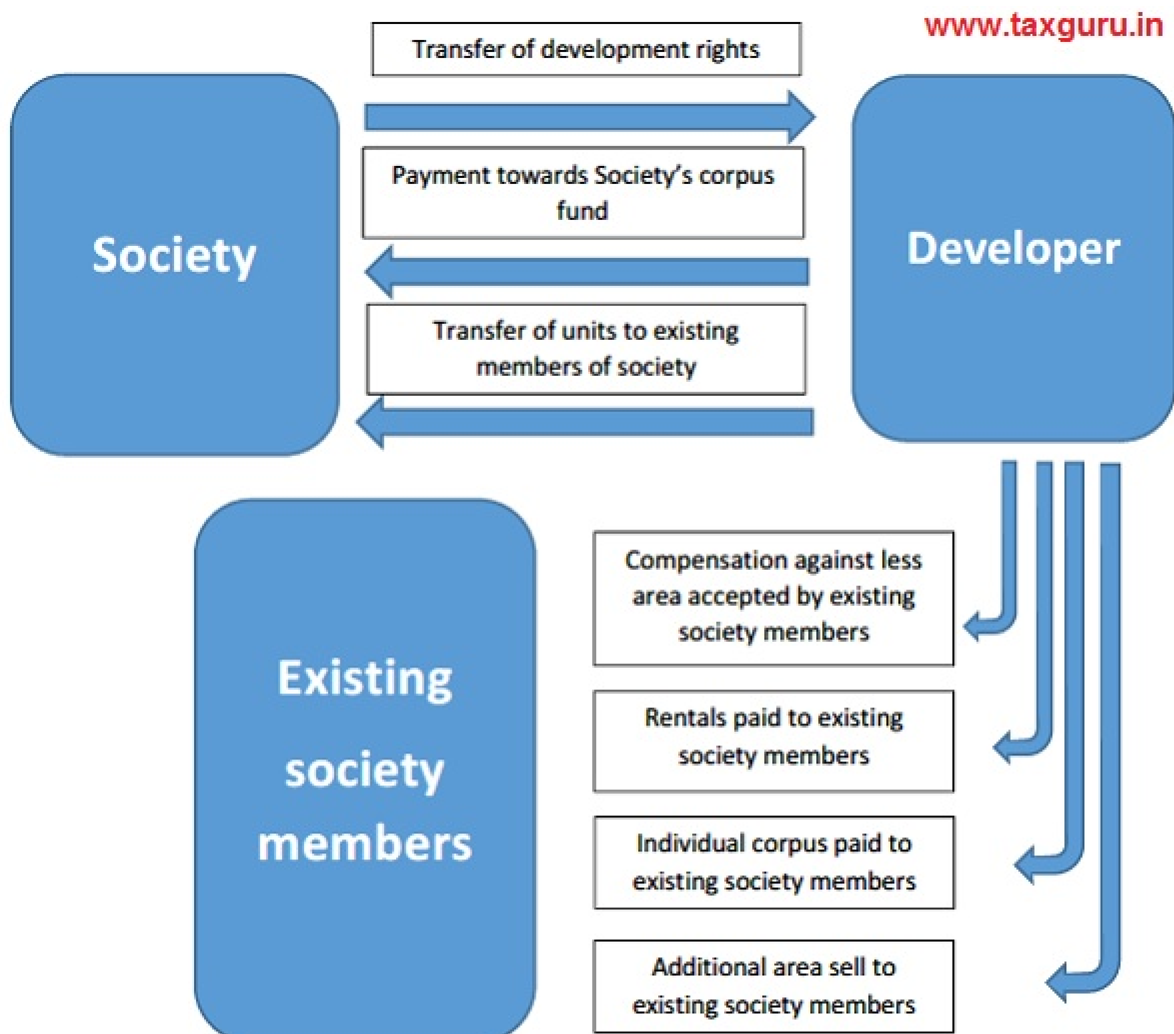
Introduction :

In the real estate industry, redevelopment agreements are often observed model. Societies, after few years of constructions, undergo redevelopment of the property. In such type of model, generally 3 parties are involved viz. society, developers and existing society members. In this article, we are going to discuss the flow of transactions, taxability and other aspects in these kinds of arrangements.

Flow of transactions :



Part I : Tax implications on 1st limb of transaction i.e transfer of development rights

1) In pre-GST regime, it was a settled principal that land includes benefits arise out of land. Various judicial pronouncements have also upheld the same view. However, in GST regime the legislative intention is to make it taxable.

2) Whether transfer of development rights can be treated as supply?

As per section 7(1) of **CGST Act, 2017**, supply includes all forms of supplies which takes color of the illustrative terms mentioned therein. The activity of **transfer** of development rights is very well covered under definition of supply.

3) Whether transfer of development rights is supply of goods or supply of services?

For the purpose of applicability of GST, there must be supply of either goods or services. As per definitions, “goods” means every kind of movable property. Definition of movable property is not provided under CGST Act, 2017. As per section 3(36) of The General Clauses Act, 1897, movable property shall mean property of every description, except immovable property.

As per section 2(102) of CGST Act, 2017, “services” means **anything other than goods**, money, and securities but includes activities relating to the use of money or its conversion by cash or by any other mode, from one form, currency or denomination, to another form, currency or denomination for which a separate consideration is charged.

As mentioned above, anything other than goods to be covered under ambit of services. Hence, the legislative principal that any benefit arising out of land will form part and parcel of land i.e immovable property is no more applicable in GST and transfer of development rights will be treated as supply of service.

4) Even if transfer of development rights are to be treated as supply of service, whether it will be covered under schedule III of CGST Act, 2017?

Schedule III contains activities to be treated as neither supply of services nor supply of goods and hence are out of ambit of GST. As per entry no. 5 of schedule III of CGST Act, 2017, **sale of land** and sale of building are not to be treated as supply of goods or services. However, in our opinion, the said entry covers only absolute **sale of land** and not the **transfer of development of rights.**

5) Legislative intention –

Notification no. 4/2018 – Central Tax (Rate) dt. 25th January, 2018, issued in exercise of powers conferred by section 148 of CGST Act, 2017. The notification specifies certain class of registered person for which special procedure to determine time of supply in case of supply of development rights has been specified.

It implies that as government is specifying Time of Supply in certain circumstances, it presumed the applicability of GST on transfer of development rights.

Considering above discussion, we can conclude that the activity of transfer of development rights is to be treated as supply of service and hence taxable under GST.

It is needless to mention that 2nd limb of transaction i.e assignment of a portion of the constructed area in the form of flats is taxable under pre-GST regime as well as in GST regime also.

6) **Other aspects : Rate of tax, Exemption, Valuation, Reverse charge mechanism, Time of supply**

a) Rate of Tax –

In the absence of any specific entry of concessional rate, such activity is taxable @18%.

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 abovementioned 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**, as follows –

(i) Monetary consideration :

In many cases, monetary consideration is payable by developer to society as a corpus fund as a consideration against development rights. Final liability to be calculated in the ratio of un-booked units as on the date of completion certificate or first occupation of project whichever is earlier.

Formula: Monetary consideration (x) area of flats remain unsold (÷) complete area of project.

(ii) Non-monetary consideration : Units given to existing society members

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.

As per paragraph 1A, value of supply of service by way of transfer of development rights by a person to the promoter against consideration in the form of residential 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 is transferred** to the promoter.

As per paragraph 1B, value of portion of residential 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.

Hence, valuation mechanism of service by way of transfer of development rights has two fold effect.

(i) Calculate value **on the date of transfer of development rights** for entire area of project considering per square foot rate of value charged for similar apartment from independent buyer **nearest to the date on which such development rights is transferred.**

The value calculated as per above mechanism pertains to complete area of the project including area of flats remain unsold. Hence, proportionate tax payable on value of flats remained un-booked is to be calculated as follows –

Value as calculated above (x) area of flats remain unsold (÷) complete area of project.

(ii) Tax payable calculated as above shall not exceed 1% of value of affordable and 5% of non- affordable apartments.

Such value shall be calculated considering per square foot rate of **value of similar 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 unbooked is to be calculated as follows –

Value of un-booked affordable flats (x) 1% (+) value of un-booked non affordable 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 shall be lower of tax calculated as per step 1 and step 2.

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, 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) and entry (b) of **notification no. 6/2019 – Central Tax (Rate) dated 29th March, 2019**, time of supply shall arise on the date of issuance of completion certificate for the project or on its first occupation whichever is earlier.

Hence, liability payable is deferred as prescribed above.

In part II of the article, we will analyse 2nd and 3rd limb of transaction.

(Above article was written on 23rd January, 2021 & 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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