



GN LAW ASSOCIATES

ARTICLES 2019



www.gnlawassociates.com

TREADING THE GST PATH – XLVII GST LIABILITY OF LANDOWNERS UNDER JOINT DEVELOPMENT AGREEMENTS

Author : G. Natarajan

Be it the erstwhile Service Tax regime or the current GST regime the issue of levy of Service Tax / GST on the builders, who undertake construction on the basis of Joint Development agreement with the landowners and hand over part of the constructed area (flats are commercial area) is always marred by confusions.

In this article, another new dimension to the issue would be discussed.

Apropos to Notification 4/2018 Central Taxes (Rate) Dt. 25.01.2018, which is reproduced below.

Special procedure for payment of CGST for construction under transfer of development rights

In exercise of the powers conferred by section 148 of the Central Goods and Services Tax Act, 2017 (12 of 2017), the Central Government, on the recommendations of the Council, hereby notifies the following classes of registered persons, namely :-

(a) registered persons who supply development rights to a developer, builder, construction company or any other registered person against consideration, wholly or partly, in the form of construction service of complex, building or civil structure; and

(b) registered persons who supply construction service of complex, building or civil structure to supplier of development rights against consideration, wholly or partly, in the form of transfer of development rights,

as the registered persons in whose case the liability to pay central tax on supply of the said services, on the consideration received in the form of construction service referred to in clause (a) above and in the form of development rights referred to in clause (b) above, shall arise at the time when the said developer, builder, construction company or any other registered person, as the case may be, transfers possession or the right in the constructed complex, building or civil structure, to the person supplying the development rights by entering into a conveyance deed or similar instrument (for example allotment letter)

The above notification has been issued under Section 148 of the CGST Act, 2017, which reads as,

148. Special procedure for certain processes. – The Government may, on the recommendations of the Council, and subject to such conditions and safeguards as may be prescribed, notify certain classes of registered persons, and the special procedures to be followed by such persons including those with regard to registration, furnishing of return, payment of tax and administration of such persons.

A reading of the above notification would reveal that for the first time, a concept of landowner providing a service of granting development rights in favour of the builder is being referred to. It has been prescribed that the landowners supplying the service of development rights to the builder and the builder supplying construction service to the landowners are liable to pay GST at the time when the possession of the constructed area meant for the landowners is handed over the landowner, through any document. For the service provided by the landowners to the builder, by way of transfer of development right, the consideration from the builder is in the form of constructed area being handed over; and for the service of construction provided by the builder to the landowner, the consideration from the landowner is the grant of development right. A barter transaction!

Two questions arising out of the above, is as to (i) how to arrive at the value of, service provided by the landowner to the builder, in the form of grant of development right; and (ii) how to arrive at the value of service provided by builder to landowner;

Before further proceeding, it is better to understand the scheme of Joint development.

Landowners who own land and Builders who have the expertise in construction would enter into a Joint Development agreement, whereby the landowner would grant the right to the builder, to develop the property into a residential or commercial property, by obtaining all approvals. For this purpose, suitable Power of Attorney would be executed by the landowner in favour of the builder. The builder would also undertake the construction at his cost. The total constructed area, would be agreed to be shared between the landowner and builder in agreed proportion.

When the builder sells his portion of constructed area, proportionate share of undivided share of land (UDS land) pertaining to such constructed area, would also be conveyed to such buyers, by the landowner. In other words, the landowner would agree to part with his ownership over the UDS land, proportionate to the builder's share of constructed area. In turn, the landowner would get his agreed share of constructed area, the UDS land pertaining to which is already owned by the landowner.

At this stage the question as to whether the landowner is providing service to the builder, in the form of transfer of development right or not, is based on the terms of the contract and has to be decided on a case to case basis. Some of the Joint Venture agreements may not envisage any such service of grant of development right by landowner to the builders, but would only for the purpose of engaging the builder for construction, on sharing of constructed area. In this article it is presumed that there is such a service by way of grant of development rights by the landowner to the builder.

The following example would further help in understanding the above.

1	Total area of land owned by the landowner	6000 Sq. Feet
2	No of flats that could be constructed in the land, by the builder	6 flats of 2000 Sq. Feet each, totaling 12,000 Sq. Feet of constructed area
3	6 flats of 2000 Sq. Feet each, totaling 12,000 Sq. Feet of constructed area	50 : 50
4	No. of flats for landowner	3
5	No. of flats for builder	3
6	Proportionate share of UDS land for each flat	1000 Sq. Feet (6000Sq. Feet / 6 Flats)
7	The total price at which the builder sells his flat, (per flat)	Rs.8,000 per Sq. Feet, (Rs.8,000 x 2000 Sq. Feet) i.e. Rs.1,60,00,000
8	Out of the above price, the price of UDS land, as per guideline value	Rs.6,000 per Sq. Feet, i.e. 60,00,000 (Rs.6,000 x 1000 Sq. Feet)
9	Value attributable to construction.	Rs.1,00,00,000, i.e. Rs.1,60,00,000 – Rs.60,00,000 (Total price minus value of UDS land)

It may be observed from the above that when the builder sells his share of 3 flats, he would get a total price of Rs.4,80,00,000 (3 Flats x 2000 Sq. Feet each x Rs.8,000 per Sq. Feet), out of which Rs.1,80,00,000 (3 flats x 1000 Sq. Feet UDS land each x Rs.6000 Sq. Feet) towards the sale price of proportionate UDS land, which is conveyed by the landowner to the builder's buyers, as per the Joint Development agreement. This amount would be retained by the builder himself, as against the 3 flats being constructed by him for the landowner. The builder is liable to pay GST for the services provided to the landowner, on an appropriate value.

The landowner would receive 3 flats from the builder. The proportionate UDS land for these 3 flats are already owned by the landowner. The value of these 3 flats (excluding UDS land), on the basis of the value charged by the builder for similar flats from his buyers, would be Rs.3,00,00,000 (3 flats x Rs.1,00,00,000, i.e out of the total price of Rs.1,60,00,000 per flat charged by the builder, Rs.60,00,000 is towards UDS land and the balance Rs.1,00,00,000 represent the value of construction)

It may be noted that the landowner has parted with UDS land of 3000 Sq. Feet, proportionate to the 3 flats meant for the builder, valued at Rs.1,80,00,000 (3000 Sq. Feet x Rs.6,000 per Sq. Feet). In turn the landowner has received 3 flats from the builder, the value of which is Rs.3,00,00,000, as calculated above. (It may be noted that the builder charges a total price of Rs.1,60,00,000 from his buyers, out of which Rs.60,00,000 pertain to the price of the UDS land. So the balance amount of Rs.1,00,00,000 represent the value of one flat excluding UDS land, in the hands of the landowner).

So, the difference between the value of 3 flats (Rs.3,00,00,000) received by the landowner and the value of UDS land parted by the landowner (Rs.1,80,00,000), i.e. Rs.1,20,00,000 represent the value of service of transfer of development right provided / supplied by the landowner to the builder. So the landowner would be liable to pay GST on Rs.1,20,00,000 @ 18 % for the services of granting development right to the builder. Such GST is eligible for ITC in the hands of builder, as it is an input service for the taxable output services provided / supplied by the builder.

It may be noted that thus the value of service of transfer of development right provided / supplied by the landowner to the builder has to be determined on a case to case basis, by comparing the total value of flats received by the landowner, minus the value of UDS land parted with by him.

To elaborate further, the landowner, parts with UDS land pertaining to builder's share of flats (which is a transaction in immovable property) and also provides the service of transfer of development right to the builder, and in turn gets his share of constructed area. The value of landowner's share of constructed area, thus represent the value of UDS land parted by him and the value of service of transfer of development right. Thus, from the total value of constructed area received by the landowner, if the value of UDS land parted by him is reduced, the balance would represent the value of transfer of development right provided by the landowner, on which is liable to pay GST.

As a corollary, the builder has provided construction services to the landowner and in turn retaining the sale proceeds from sale of UDS land pertaining to his share of flats, which is the value on which he is liable to pay GST. i.e. the value of service provided by the builder to landowner would be Rs.1,80,00,000 i.e. sale proceeds of UDS land pertaining to builder's share of flats retained by him.

To put it simply,

(i) The builder provides service of construction to the landowner and in turn retained the sale proceeds of UDS land pertaining to his share of flats, i.e. Rs.1,80,00,000, which is the value of service provided by builder to landowner, on which the builder is liable to pay GST.

(ii) The landowner can avail ITC of this GST, if he in turn sells these flats to buyers identified by him, on payment of GST.

(iii) The landowner parts with his UDS land pertaining to builder's share of flats and also provide the service of transfer of development right to the builder and in turn gets flats worth Rs.3,00,00,000. After reducing the value of UDS land parted with by him, i.e. 1,80,00,000, the value of service of transfer of development right provided by him would be Rs.1,20,00,000, on which the landowner is liable to pay GST.

(iv) The builder can claim ITC of this service tax charged by the landowner.

(Published in www.taxindiaonline.com)

