

DEVELOPMENT AGREEMENTS- AREA SHARING AND REVENUE SHARING-TAX ISSUES

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The transfer of immovable property by owners of land through the developers and/or his nominees using the mechanism of a Development Agreement (popularly known as a Joint Development Agreement) has been rampant especially in prime urban areas where the Owners but do not have the time or expertise to develop the land and market the property on their own and therefore enter into an arrangement of mutual benefit with a reputed builder known as a Developer for developing and marketing the development to various buyers of individual units. The Development Agreements are either entered into under the Area Sharing Method or the Revenue Sharing Method.

A. Broad Features of Area Sharing Development Agreements:

i. Owner of lands:

A Single Owner being an individual or an entity or a group of Co-Owners own certain lands.

ii. Conversion:

Such lands may be agricultural in nature and they get 'converted' by suitable orders of the competent statutory authorities for use for non-agricultural purposes i.e., for the development of sites, flats, apartments, townships etc.

iii. Offer of developer:

A Property Developer approaches the Owners and offers the following: -

- a. To construct for the Owners certain specified extent of built up area of flats / apartments together with the right to use certain common areas, facilities and amenities.
- b. In return for the same, the Owner agrees to sell a specified share / percentage of undivided interest in the land to the prospective buyers nominated by the Developer.

iv. Acceptance and execution of development agreement:

The aforesaid terms are accepted by the Owners and in pursuance thereof the Development Agreements are entered into between the Owners and the Developers. Under these agreements the Developer by himself does not purchase any immovable property from the Owner and it is the prospective buyer who buys a specified share of undivided interest in the land from the Owner or Developer as the case may be. Therefore, these agreements between the Owner and the Developer are purely contractual and commercial in nature and hence logically the provisions of Section 53A of the Transfer of Property Act, 1882 should not apply since the Developer by himself is not a transferee / purchaser of any immovable property. Further the development agreement is more in the nature for a "contract for sale" and not a "contract of sale".

v. Popularly known as Joint Development:

Even though it is only the Developer who develops the property and constructs the super structure, is responsible for all the risks and obligations attached to the development, the above arrangement is popularly known as "Joint Development".

vi. Developer to nominate buyers:

The Developer is authorized to exclusively nominate the prospective buyers for his share of super built area known as "Developers Share", and enter into agreements with them fixing the sale price/s and consideration payable by them.

vii. G.P.A to Developer:

The Developer is empowered through a General Power of Attorney (GPA) by the Owner to act on Owner's behalf and agree to sell certain specified shares of undivided interests in the land to the prospective buyers at the aforesaid prices fixed for this purpose. A General Power of Attorney given by the Owner to a Developer constitutes only an authority given to a Developer to act for and on behalf of and in the name of the Owner. No right or interest in the immovable property or right to have possession of the property is conferred on the Developer in any manner whatsoever. The GPA also empowers the Developer to do all acts, deeds and things in pursuance of the Development Agreement including applying for plan sanction, various licences and clearances required for the development of the Project.

viii. No power given to Developer to execute Sale Deeds and possession to prospective buyers before sale:

The Developer is not given any power to execute sale deeds/ lease deeds/ mortgage deeds etc in favour of the prospective buyers and /or others but only given the power to enter into agreements and collect advances from the prospective customers. Such power to execute sale deeds etc is conferred on the Developer on completing the construction of the specified built up area of flats / apartments for the Owner as per the agreed specifications and dimensions, and on handing over the same to the Owner with 'occupancy' rights on or after being granted by the competent statutory authorities. At this stage the sale deeds are executed by the Owner himself in favour of the prospective buyers or in the alternative, only at this stage the Owner gives a separate General Power of Attorney to the Developer to execute and register the sale deeds on Owner's behalf to and in favour of the prospective buyers. At no stage before the actual sales are effected, the prospective buyers are put in possession of the flats / apartments sold to them.

ix. Allocation/ Area Sharing Agreement

The Owner and the Developer will enter into area sharing/allocation agreement immediately after the receipt of plan sanction. In the said agreement, the Parties will clearly identify the units which will be allotted to the Developer as a part of Developer's share and to be allotted the Owner as a part of the Developer share. Such allocation can also be done Block-wise, Floor-wise or Unit-wise.

x. Developer's right to entry is only 'License' – not possession:

It will be specifically provided that the development and construction and such right of entry is only a License coming within the purview of the provisions of Section 52 of the Indian Easements Act 1882. It will be clearly provided and recorded that the legal domain, control and physical possession of the property shall be vested with and remain with the Owner till the same or parts thereof are sold to the prospective buyers.

The Developer is only permitted to enter the property for the limited purpose of development. The Developer not being the purchaser or a transferee, the provisions of Section 53-A of the Transfer of Property Act 1882 should have no application and the aforesaid right of entry to the Developer constitutes only a 'License' coming within the meaning of the term under the aforesaid Section 52 of the Indian Easements Act 1882.

xi. Separate agreements for flats / apartments:

The Developer enters into separate agreements for construction with the prospective buyers fixing the consideration payable by them for the super built area in respect of the Developers share which devolves upon the Developer as per the development agreement. These agreements are entered into by the Developer on his own and not as a G.P.A holder for the Owner. Further the Developer also enters an agreement of sale of undivided share of right, title and interest in land in favour of the prospective buyers of apartments where he acts in the capacity of the GPA holder for and on behalf of the Owner and also himself joining the said agreement as a confirming party.

xii. Registration of Agreements – Benefits Available:

The Development Agreements entered into by the Owners with the Developers can be registered with the appropriate registration authorities of the State Government under the Registration Act 1908, and they will get the benefit of entry into Book-I maintained in the Registrar's Office. Such entry will ensure that there is 'public notice' to these documents and their contents. Whenever any encumbrance certificates are obtained on the concerned immovable properties, there will be entries recording the execution of the Development Agreement. The General Power of Attorney (GPA) given to a Developer by the Owner can also be registered in the same manner and the same will be entered in Book IV maintained at the Sub Registrar's office. When the fact of this G.P.A is recorded in the Development Agreements, there will be 'Public Notice' to the G.P.A also. As the G.P.A's are given to the Developer for 'consideration', these G.P.A's will become irrevocable as it will be treated as creating an agency coupled with interest to come within the purview of the provisions of Section 202 of the Indian Contract Act 1872. There will be a suitable clause in the G.P.A to indicate that the same is irrevocable. The total cost of stamp duty and registration fee payable on development agreements and the general power of attorney granted in pursuance to the same vary in different states. Generally, the stamp duty payable on the GPA is nominal if the appropriate full stamp duty is paid on the Development Agreement and vice versa.

B. Main Points Relating to Taxation Highlighted:

- i. The Developer is not a Transferee / Purchaser coming within the meaning of Section 53A of the Transfer of Property Act 1882.
- ii. The Developer does not buy any land or property from the Owners.

- iii. The right to develop the property granted to a Developer as provided in the Development agreement does not constitute a contract to a transfer of any immovable property as between the Owner and the Developer, to attract the provisions of Section 53-A of the Transfer of Property Act 1882 between them.
- iv. The Development agreement is a "contract for sale" and not a contract of sale" and hence there is no interest created on the property per se in favour of the Developer.
- v. The Developer only nominates the prospective buyers for his share.
- vi. The Developer enters the property only for the purposes of development of the property under a licence issued which is of the nature prescribed u/s 52 of the Indian Easements Act 1882 and not as a purchaser / transferee.
- vii. The G.P.A given to a Developer is only to enter into agreements with the prospective buyers for and on behalf of the Owner and not for executing the sale deeds. There will be a restrictive clause in the G.P.A to this effect.
- viii. Only the prospective buyers are the purchasers / transferees in respect of the flats / apartments purchased by them together with the corresponding shares of undivided interests, rights and titles in the land.
- ix. The prospective buyers of flats / apartments are never put into possession of their apartments before the sale deeds are executed and registered in their favour and hence there is no scope for invoking the provisions of Section 2(47)(v) read with Section 45 of the Income tax Act 1961 and the provisions of Section 53-A of the Transfer of Property Act 1882.
- x. It is only the Developer who develops the lands by constructing flats/ apartments together with common ways, infrastructure, amenities and facilities both for the Owners of lands as well as for the prospective buyers of flats/ apartments and his profit margins is assessable as business income.
- xi. **In the hands of the Owners, the chargeability to tax the gains made by them will be treated as follows: -**
 - a. Normally only as and when the flats / apartments constructed by the Developer towards the Owners share are handed over to the Owner post completion, the Owner hands over the legal possession of the Developers share to the Developer

and/or his/its nominees and at this point of time the Owner becomes liable to pay Capital gains on the transfer of the land pertaining to the Developers share . The deemed value of consideration for the transfer of the Developers share of land to the Developer and/or its/his nominees to the Owner, will be equal to the cost of the flats / apartments built by the Developer for the Owners. On the occupancy of these flats / apartments being given to the Owners after the completion of the construction of the same as per the specifications and dimensions mutually agreed to between the Owners and the Developer, the consideration to be given to the Owners becomes fully /discharged.

- b. When the Owners get more flats / apartments than what they can personally use and occupy, they affect sales of such additional flats / apartments. When such sales are made the following position will emerge.
- c. If the sales are made within two years (earlier three years) from the date when occupancy was given to the Owners, the further gains made by them on sale of the super built up area will be treated as short term capital gains and if the sale of the super built up area is effected after a period of three years after taking possession, the gains will be treated as long term capital gains. However, it is to be noted that the consideration for the sale of undivided share of land relating to the Owners share of apartments will be taxed as long-term capital gains only as the same were always held by the Owners and not transferred at any time to the Developer or his nominees.

There is a credible argument to also treat the transfer of the super built area i.e., the units belonging to the Owners share as long term capital gains even if the same were to be sold(transferred) immediately after receiving possession from the Developer to the ultimate Buyer(transferee), on the ground that the right to receive a specific identified super built up area fructified and crystallised as on the date of entering into the Allocation Agreement/Area Sharing Agreement between the Owner and the Developer. In this regard there are a catena of decisions which have held that the period of holding for the purpose of determining the capital gains arising from sale/transfer of a capital asset should be reckoned from the date on which he had a right in the capital asset, which could either be the date of Agreement or Allotment of a unit. The decisions to be referred to in this regard are as follows:

Allotment of flat to Assessee results in Conferment of Rights to the Assessee in the property and period of holding is to be reckoned from the date of allotment of Flat.

- Madhu Kaul v. CIT & Anr. (2014) 57 (I) ITCL 306 (Punj & Har-HC) : (2014) 363 ITR 54 (Punj & Har)
- Vinod Kumar Jain v/s CIT (2012) 344 ITR 501 (P& H)
- ITO Vs Jayshree H Jain (2016) 150 TR (A) 758 (Mum-Trib).
- ACIT v. Keyur Hemant Shah (2019) : (2019) 72 ITR (Trib) 108 (Mum-Trib) (2019) 199 TTJ (Mum-Trib) 388
- Gurucharansingh Anand v. Dy.CIT (1993) 45 ITD 299 (JP-Trib) Jaipur Bench
- Asstt.CIT v. Nagesh C Kawale (2001) 73 ITD 38 (Pune-Trib)
- Awadhinarayan Lakshminarayana Singh vs. DCIT, ITA No. 5555/Mum/2017, ITAT "A" Bench Mumbai, rendered on 12/12/2018.
- DCIT vs Jennifer Chakraborty (2018) ITA no 400/Kol/2016 and ITA no 514/Kol/2016 rendered on 31st July 2018.
- ACIT Central Circle 16(2) Mumbai vs Ashwin Bhalekar ITA no 6822/Mum/2016 (ITAT Mumbai "A" Bench) rendered on 21-5-2019
- CIT vs Ram Gopal (2015) 55 taxmann.com 536 (Del)
- ITO V/S Monish Kaan Tahilramani ITA No 4715 / Mum / 2015 ITAT Mumbai Bench Rendered ON 2/04/2019
- CIT V/S Tata Teleservices Ltd (1980) 122 ITR 594 (Bombay)
- CIT V/S Sterling Investment Corporation Ltd 123 ITR 441.
- Sanjeev Lal & another vs. CIT (2014) 365 ITR 389 (SC)

It has also been held that the allotment of an apartment is by itself a right acquired by the allottee in the apartment and in case of transfer of such right by the allottee after the period of 3 years the same will be considered as transfer of long term capital asset with capital gains applicable accordingly.

- Miss Indira Vasanji Shah v. DCIT (2017) ITA No.8805/Mum/2011
- Bhagwan J Tahilliani (HUF) vs. ITO, [2018] 67 ITR (S.N.) 38 (Mumbai ITAT)

Allotment right will commence from the date from which the agreement in pursuance of the allotment letter is entered into and not from the date of the allotment or confirmation letter.

- Gulshan Malik v CIT (2014) 223 Taxman 243 (Del).

xii) Claiming of deduction under Section 54F by the Land Owner

Where the Owners retain one flat each out of the total number of apartments allotted to them towards their share, each of them will be entitled to claim exemption under Section 54F of the Income tax Act on the cost of construction of such retained apartment, subject however to other conditions under Section 54F being fulfilled by them.

In another interesting decision in the case of **Vittal Krishna Conjeevaram V ITO (2013) 144 ITD 325 (Hyd "A" Trib)**, the tribunal has held that where an Owner received seven flats in exchange for the portion of land being a residential property in pursuance to a development agreement, he was entitled to a deduction u/s 54F in respect of all seven flats received following the decisions of the Karnataka and Andhra Pradesh High Courts referred above. The analogy adopted in the above decision has also been affirmed by the Madras High Court in **CIT Coimbatore Vs Smt V R Karpagam (2014) 50 taxmann.com 55** rendered on 18th August 2014 also reported in **(2015) 373 ITR 127 (Mad)** and by the **ITAT "A" Bench Chennai in the case of ITO Business Ward V (1) Chennai Tribunal vs PA Sarala (2015) 58 taxmann.com 290** rendered on 15-5-2015.

The other case laws that have upheld the analogy rendered by the above decisions are detailed below:

- CIT v. Smt K.G Rukminiamma 331 ITR 211 (Kar-HC)
- CIT Vs. Gumanmal Jain (2017) 394 ITR 666 (Mad)
- ITO v. Sureddy Venkata Ramanamamma (2017) 165 ITD 574 (Vishaka)
- Dr, Sudhir Naik and others vs ITO, 4(2) Hyd ITA No. 1463 and 1467/Hyd/2016 ITAT "A" Bench rendered on 31/01/2018.
- Harbinder Singh Chimni v. Dy. CIT [2018] 68 ITR (Trib) (S.N.) 73 (Delhi)
- Meghraj Singh Shekhawat v. Dy. CIT I. T. A. Nos. 443 and 444/JP/2017 dated March 7, 2018.
- Damodar Reddy Vs. ITO ITA No. 3052/Bang/2018 rendered on 9 January, 2019 (ITAT, BANGALORE BENCH)
- B J Badrinath v. ITO (2019) 168 TR (A) 820 (Ban Trib) Ward 4(3)(1)- ITA No. 2938/Bangalore/2018 rendered on 16/11/2018 (ITAT "SMC, C" Bench : Bangalore)

- A.R. Prasad v. ITO Ward 6(2)(4) and A.P. Lakshmi Gowri v. ITO ward 6(2014) ITA no. 956 & 957 (Bangalore) 2016 rendered on 28/08/2019 ITAT Bangalore Bench at Bangalore.

These decisions may however not be relevant any more with the amendment to the provisions of Section 54 and 54F by the Finance Act 2014 where it is now clearly mandated by law that the assessee will be entitled to exemption to the extent of investment in "one house" only

C.TRANSFER TAKES PLACE ON THE DATE OF SIGNING THE DEVELOPMENT AGREEMENT

However, it is pertinent and relevant to state that in spite of all the basic concepts mentioned above indicating that there cannot be a “transfer” on the date of entering into the joint development agreement, **a spate of decisions rendered by various courts and tribunals which are detailed below, have held that there is a “transfer” to the extent of the Developers Share in the land as on the date of entering into the Joint Development agreement itself.** The decisions have been rendered on the analogy that the Developer has been given unrestricted and unbridled right to enter into Agreements for Sale and even Sale Deeds in respect of his/its share of units, the right to mortgage his/its share of units for construction finance thereby indicating that the domain and control of the immovable property to the extent of the Developers Share is already transferred to and vested with the Developer as on the date of entering into the Development Agreement.

The decisions to be referred to in this regard are as under:

The Karnataka High Court has vide its judgement rendered on 20th June 2011 in the case of **CIT Vs Dr T K Dayalu in ITA No 3209 of 2005 C/W ITA No 3165 of 2005, 60 DTR (Kar) 403, 202 Taxman 531(Kar), following the decision of the Bombay High Court in the case of of Charturbuj Dwarakadas Kapadia Vs CIT (2003) 260 ITR 491 (Bom),** held that the “transfer” as far as the Owner is concerned takes place on the date of entering into the development agreement on the ground that possession given to a Developer would also fall into the ambit of the definition of “transfer” u/s 53A of the transfer of Property Act 1882 r/w Section 2(47)(v) of the Income Tax Act. This judgement with due respect seems to be flawed as it has not considered the basic fact that the possession given to a Developer is permissive possession and cannot be construed as a possession given in part performance of a contract of the nature referred to in Section 53A of the Transfer of Property Act.

The Karnataka High Court has in the case of CIT and Others Vs H B Jairaj (2012)43(I) ITCL 85 in ITA No 20 of 2005 C/W ITA No 21 of 2005 rendered on 16th September 2011, held that the date of entering into the Development agreement should be reckoned as the date of "transfer" of land to assess the Capital Gains arising to the Owner, thereby confirming the principle laid down in Dr TK Dayalu's decision as above and has further followed the said principle in the case of CIT Vs Ved Prakash Rakhra (2012) 210 Taxman 605 Karnataka: (2013) 256 CTR (Karn) 285. The analogy of the Karnataka High Court in the case of Dr.T.K. Dayalu and H.P.Jayaraj (Supra) has been followed by the said court in the case of Smt. Prameela Krishnan vs. Income Tax Officer, Ward -1(2) Mysore vide judgement dated 18/11/2013 reported in [2014] 42 taxmann.com 185 Karnataka and (2014) 221 Taxmann 418(Kar).

The Bangalore ITAT "A" Bench has in the case of ITO v/s M.S Nagaraj ITA No. 676/Bang/2011 vide its judgement rendered on 01.12.2014 reported in 52 taxmann.com 511 confirmed the analogy of the decisions in the case of Dr. T.K Dayalu and Ved Prakash Rakhra (Supra), by holding that the "transfer" takes place on the date of entering into Joint Development and the consideration for the purpose of transfer is the cost of construction to be incurred by the developer on the Owner share of super built up area. It is important to note that this judgement all though rendered after the provisions of Section 50D came into force relates to an assessment year which is prior to the year in which Section 50D was introduced.

The Tribunal in rendering its decision has also cited the decisions of the Madras High Court in the case of T.V Sundaram Iyengar and Sons 37 ITR 26 and that of the Apex Court in the case of Alapathi Venkataramiah v/s CIT (1965) 57 ITR 185(SC). In the said case the Hon'ble court has observed that to attract the liability to tax under Section 45, it is sufficient if in the accounting year, profits have arisen out of the transfer of capital assets and the assessee had a right to receive the profit. The court also held that the actual receipt of profit is not a relevant consideration.

The Hyderabad Tribunal in the case of ACIT Vs A Ram Reddy(2012) 23 Taxmann.com 59 and reported in 52 SOT 521 (Hyd B Trib) has held that the date of entering into the development agreement is the date regarded as "transfer" u/s 2(47)(v) of the Income Tax Act 1961, as the Developer has got general control over the property to use it for the intended purpose based on the earlier judgement of the Hyderabad Tribunal in the case of Dr Maya Shenoy (2009)124 TTJ 692(Hyd) and that of the Bombay High Court in the case of of Charturbuj Dwarakadas Kapadia Vs CIT (2003) 260 ITR 491 (Bom). The decision in the case of Ram Reddy (supra) has been further followed by the Hyderabad Tribunal in the case of Krishnakumar D Shah (HUF) vs

DCIT(2012) 23 taxmann.com 111 and in the case of Ravinder Singh Arora vs ACIT 10(1) Hyderabad rendered on 20th of July 2012(ITA Appeal Nos 58&355(Hyd) of 2011 and in the case of Mrs Durdana Khatoun Vs ACIT(2013) 24 ITR 55(Hyd B Bench) rendered on 5-3-2013.

The decision of the Andhra Pradesh High Court in the case of **Potla Nageswar Rao Vs DCIT IITA 245 of 2014 rendered on 9-4-2014 reported in (2014) 365 ITR 249 (AP), (2014) 269 CTR (Hyd) 325**, also supports the view adopted in the above cases.

Other decisions which have upheld the aforesaid analogy are given below:

1. Mahesh Nemichandra Ganeshwade vs. ITO (2012) 17 ITR 116 (Pune 'A' Trib)
2. Krishnakumar D Shah (HUF) Vs DCIT(2012) 23 taxmann.com 111
3. Jasbir Singh Sarkaria (2007) 294ITR 196(AAR)
4. Azad Zubarchand Bhandari Vs Asst CIT(2013) 58 SOT 347 (Mum 'A' Trib)
5. Taher Alimohammed Poonawala v. Addl. CIT [2009] 124 TTJ (Pune) 387- ITAT Pune Bench
6. Ms Rubab M Kazerani Vs Jt CIT(2005) 2(II) ITCL 456(Mum-Trib)(TM)
7. ITO Vs Vikash Behal (2010) 34(II) ITCL 73 (Kol "C" Trib)
8. G Sreenivasan V Dy CIT (2013) 140 ITD 235 (Coch-Trib)
9. R Kalanidhi Vs ITO (2009) 314 ITR (AT) 266 (Chennai-ITAT)
10. DCIT Vs Jai Trikanand Rao (2014)149 ITD 112 (Mum J Trib)
11. Ram Prasad Vs Dy CIT (2015) TaxPub(DT) 5142 (Hyd 'A' Trib)
12. B V Narayana Reddy v. Asst CIT (2015) TaxPub (DT) 4553 (Hyd 'B' - Trib)
13. ITO Vs Ayisha
14. Fathima (2016) 160 ITD 377 (ITAT Chennai Bench D): (2016) 182 TTJ(ITAT Chennai Bench D) 437
15. Adinarayana Reddy Kummata vs ACIT Circle-11(1), Hyderabad [2018] 91 taxmann.com 360 [Hyderabad-Trib.].
16. CIT v. Jeelani Basha (2002) 256 ITR 282/122 Taxman 509 (Mad)
17. Tamilnadu Brick Industries V ITO ITA no 744/Chny/ 2017 rendered on 11-5-2018
18. [Kasturi D v CIT 323 ITR 40 \(Mad\)](#)
19. Udai Hospitals Pvt Ltd vs ITO. Ward 17(3), Hyd, (ITAT "B" Bench) ITA No. 1755/Hyd/2017 rendered on 28/09/2018.
20. K Vijaya Lakshmi Vs ACIT ITA no. 1561/Hyd/2016 and 372/Hyd/2017 rendered on 28/02/2018.

21. K. Vijaya Lakshmi Vs ACIT (2019) 165 TR (A) 253 (Hyd-Trib): (2018) 195 TTJ (Hyd 'B' - Trib) 114
22. Vijaya Productions (P) Ltd vs Addl. CIT (2012) 134 ITD 19 (Chennai-Trib)(TM)
23. Dy. CIT vs. Jamnaben J Gokani 2015 TaxPub(DT) 1224 (Mum 'E' - Trib)
24. ITO vs. Arvind Govardhan & Others (2018) TaxPub DT 235 (Bang 'A' - Trib): 61 ITR (Trib) 159 (Bang 'A' - Trib)
25. Damodar Reddy Vs. ITO ITA No. 3052/Bang/2018 rendered on 9 January,2019 (ITAT, BANGALORE BENCH)

It is respectfully submitted that the adverse decisions as detailed above have emanated purely as a result of faulty documentation and lack of proper representation before the judicial authorities. The critical aspect that there has to be a definite value for the consideration as on the date of transfer and other critical aspects has not been put forth properly and effectively during the judicial proceedings.

The credible arguments which could have been put forth before the relevant judicial authorities and which could now be canvassed before the apex court are as follows-

a) The following observation of the Supreme Court in the case of **Govind Saran Ganga Saran v/s Commissioner of Sales Tax and Others (1985) 155 ITR 145 (SC)** is worth considering

The Components which enter into the concept of a tax are well known. The first is the character of the imposition known by its nature which prescribes the taxable event attracting the levy, the second is a clear indication of the person on whom the levy is imposed and who is obliged to pay the tax, the third is the rate at which the tax is imposed, **and the fourth is the measure or value to which the rate will be applied for computing the tax liability.** If those components are not clearly and definitely ascertainable, it is difficult to say that the levy exists in point of law. **Any uncertainty or vagueness in the legislative scheme defining any of those components of the levy will be fatal to its validity.**

It is well settled that when the language of the statute is clear and admits of no ambiguity, recourse to the Statement of Objects and Reasons for the purpose of construing a statutory provision is not permissible.

b) The following observation of the Supreme Court in the case of **Her Highness Maharani Shantidevi P Gaikwad vs. Savjibhai Haribhai Patel AIR 2001 (SC) 1462 (2001) 5 SCC 101** involved a Development agreement between an Owner and a

Developer for development of a large tract of land into a housing scheme complying with the Urban Land Ceiling Act. A Power of Attorney expressly made irrevocable was also made by the Owner in favour of the Developer. Holding that the agreement was validly terminated under the terms of the agreement, the court observed that "Section 202 had no applicability"; thus making powers under the Power of Attorney subservient to the terms of the agreement. The Court also observed:

" It is not a case of agency coupled with interest. No interest can be said to have been created on account of plaintiff being permitted to prepare the scheme and take ancillary steps".

An agreement with the Developer under which he will develop the land does not create interest in the property to be developed. Such contract itself can be terminated under circumstances. Hence a Power of Attorney given to a Developer for giving effect to an earlier agreement of development is not coupled with interest and is not irrevocable. The rights of the Developer flow from the development agreement. If stated as irrevocable, and is revoked, the agent can claim compensation.

c) To highlight this analogy the following observations of the Supreme Court in the case of **Ishikawajima - Harima Heavy Industries Ltd. Vs Director of Income Tax, Mumbai (2007) (SC) 288 ITR 408** is reproduced below:

In construing a contract, the terms and conditions thereof are to be read as whole. A contract must be construed keeping in view the intention of the parties. No doubt, the applicability of the tax laws would depend upon the nature of the contract, but the same should not be construed keeping in view the taxing provisions.

d) Section 53A of the Transfer of Property Act 1882 provides that where any person contracts to transfer for consideration any immovable property by writing, signed by him or on his behalf from which the terms necessary to constitute the transfer can be ascertained with reasonable certainty, **and the transferee has, in part performance of the contract**, taken possession of the property or any part thereof, or the transferee, being already in possession, continues in possession in part performance of the contract and has done some act in furtherance of the contract, and the transferee has performed or is willing to perform his part of the contract, then, notwithstanding that the contract, though required to be registered, has not been registered, or where there is an instrument of transfer, that the transfer has not been completed in the manner prescribed therefore by the law for the time being in force, the transferor or any person claiming under him shall be debarred from enforcing against the transferee and persons claiming under him any right in respect of the property of which the transferee has

taken or continued in possession, other than a right expressly provided by the terms of contract:

Provided that nothing in this section shall affect the rights of a transferee for consideration who has no notice of the contract or of the part performance thereof.

In the case of a development agreement whether the developer can be considered as a "transferee" or only the end buyer of apartments can be considered as a "transferee" is the critical point for evaluation.

e) The language of Section 54 of the Transfer of Property Act which provides that "sale" is as a "transfer" of ownership in exchange for a price paid or promised or part paid and part promised.

Contract for sale- A contract for the sale of immovable property is a contract that a sale of such property shall take place on terms settled between the parties.

It does not, of itself, create any interest in or charge on such property.

It is highly relevant to note that a Development Agreement is a "contract for sale" and not a "contract of sale".

The Apex Court has in the case of **Suraj Lamp & Industries (P.) Ltd v State of Haryana - 14 taxmann.com 103 (SC) [2011]** that immovable property can be legally and lawfully transferred/conveyed only by a registered deed of conveyance and General Power of Attorney Sales ('GPA Sales') or Sale Agreement/General Power of Attorney/Will transfers ('SA/GPA/WILL' transfers) do not convey title and do not amount to transfer, nor can they be recognized as valid mode of transfer of immovable property.

f) Interestingly, the High Court of Karnataka had in the case of **CWT and another Vs Giridhar G Yadalam reported in (2010) 325 ITR 223 (Karn)** held that in case of the assessee who had given his property on Joint Development, the land in question continue to be held an urban land, even though construction has commenced. It further held that the same would be the position till the construction was complete and owner's share of super built up area was handed over to him. The assessee has successfully argued before the CIT (Appeals) and the Tribunal that the land offered for Joint Development would not fall under the definition of asset under Sec 2(e)(a) of Wealth Tax Act 1957, once the construction commences on the property one of the arguments put forth by the assessee was that it had retained the ownership of the land till the flats were fully constructed and possession of assessee's share handed over to it. The said argument has in a way been upheld by the High Court by confirming the analogy that

Wealth Tax has to be paid by the assessee on the land in question by treating the same as urban land till the construction was complete. **The assessee's appeal against decision of Karnataka High Court has been rejected by the Supreme Court (2016)284 CTR 433: (2016) 237 Taxmann 392: [2016] 384 ITR 52;** thereby bringing finality to the proceedings and upholding the decision of the High Court that the Owner would have to pay wealth tax on the entire land even after construction has commenced on the property pursuant to entering the joint development agreement.

This decision could be used to counter the decisions of various High Courts which have held that there is a transfer by the owner to the developer to the extent of developer's share in the land as on the date of entering into the Joint Development.

D.TAXATION ON TRANSFER OF DEVELOPER'S SHARE IN CASE OF UNREGISTERED DEVELOPMENT AGREEMENT

It is to be noted that the document containing contracts to transfer for consideration any immovable property for the purpose of Section 53-A of the Transfer of Property Act, 1882 (4 of 1882) shall be registered if they have been executed on or after the commencement of the Registration and Other Related Laws (Amendment) Act, 2001 and if such documents are not registered on or after such commencement i.e w.e.f 24-9-2001, then, they shall have no effect for the purposes of the said Section 53-A. As a result of the said amendment it is now mandatory to register the agreement for sale and pay the Stamp duty as stipulated under the relevant article of the Schedule to the Stamp Act as if the same is not done, there will be no "transfer "of the nature referred to in Section 53-A of the Transfer of Property Act so as to invoke the provisions of Section 2 (47)(v) of the Income Tax Act. This analogy has been upheld by the Kerala High Court in the case of **N.A. Baby vs Dy. CIT (2015) 234 Taxman 371.**

The Punjab and Haryana High Court has in the case of **G S Atwal vs CIT Ludhiana rendered on 22-7-2015 and reported in (2015) 59 taxmann.com 359** held that there cannot be a transfer on the date of entering into the Joint Development agreement if such agreement is not registered pursuant the amendment to Section 17 of the Indian Registration Act 1908 as stated above. **The Supreme Court had however granted special leave to the revenue against the aforesaid decision as reported in (2015) 383 ITR (St) 1.**

The above analogy of the Punjab and Haryana High Court has been followed by the same court in the case of **Punjab Coop House Building Society V CIT and Another (2016) 386 ITR 116 (P&H)**, wherein the court has held that the possession given to the developer is only a licence and does not amount to a transfer under section 53A of the

transfer Of Property Act 1882 and consequently does not fall within the ambit of the provisions of Section 2(47) (v) of the Income Tax Act. It must be mentioned that this was a case where disputes arose between the Owners and the Developers pursuant to entering of the joint development agreement and part of the land was not given possession to the Developer.

The Mumbai Tribunal has in the case of **Fardeen Khan Vs ACIT 11(1) Mumbai- ITA No 1588/1589 of 2013 (ITAT F Bench Mumbai) rendered on 25-2-2015** has held that the provisions of Section 53A of the Transfer of Property Act read with Section 2 (47)(v) of the Income Tax Act will not apply on agreements which are not registered after the amendment to Section 17 of the Registration Act although another bench of the same tribunal had in the case of **Suresh Chandra Agarwal Vs. Income-tax Officer, Ward 20(3)(3)* rendered on 14/09/2011 (IT Appeal Nos. 2376 & 2377(Mum.) of 2010(2011)15 taxmann.com 115(Mumbai-Trib))** ,held that the amendment made by the Registration and Other Related Laws (Amendment) Act 2001 which mandates the registration of the document contemplating the transfer of immovable property for it would be construed as a part performance u/s 53A of the Transfer of Property Act, shall not affect the definition of “transfer” u/s 2(47)(v) of the Income Tax Act

In other words, according to the above judgement even if the agreement to sell with possession is not registered after 24/09/2001, it would still be considered as a ‘transfer’ u/s 2(47)(v) of the Income Tax Act 1961. This could be used by an assessee where the development agreement has not been registered.

The view that an unregistered Joint Development Agreement does not give rise to a taxable event as on the date of entering into the Development Agreement has been finally settled by the order of the Apex Court in the case of -CIT v. Balbir Singh Maini (2017) 398 ITR 531 (SC).

E. OWNERS CAN CONVERT THE LANDS INTO STOCK-IN-TRADE:

It is to be noted that all the adverse decisions have been rendered on the analogy that there is a “transfer” of a “capital asset” as understood under Section 2 (47) (v) and/ or 2 (47) (vi) of the Income Tax Act. It is to be noted that the definition of “transfer” under Section 2 (47) does not apply to a transfer of stock-in-trade as it is purely in relation to a transfer of a “capital asset” and in the absence of a specific or deeming provision, the transfer of such stock-in-trade would occur only when the risks and rewards of ownership is being transferred under the general law. Consequently, to avoid the effect of the above adverse decisions rendered in the context of “Capital Asset” as detailed in

Para C above, the Land Owner can opt to convert the land and treat the same as stock in trade in his/its books

It is to be noted that the above treatment of lands of the Owners as stock-in-trade will avoid all the risks and problems arising out of such interpretations that an agreement to sell and/or a development agreement by itself constitutes a 'transfer' within the meaning of Section 2(47)(v) read with Section 45 of the Income tax Act 1961 as held by the **Bombay High Court in the case of Charturbuj Dwarakadas Kapadia Vs CIT (2003) 260 ITR 491 (Bom) and several other decisions as cited earlier**. There will be no scope for invoking the provisions of Section 2(47)(v) and (vi) in such cases as they will be governed by the provisions of Section 2(47)(iv) read with Section 45(2) only.

- i. It is possible for the Owners to treat their lands as stock-in-trade of a business in property transactions carried on by the Owners before they enter into development agreements with the Developers. It is to be noted that the assessee should do a positive act to evidence the conversion of a capital asset and its treatment as stock in trade as held by the Allahabad High Court in the case of **Amrit Corp Limited Vs Addl CIT (2014) 226 taxmann 1(All HC)**.
- ii. In the case of self development as the individual would be undertaking an organized systematic activity of development and sale, the individual could be construed as having undertaken an activity which is an "adventure in the nature of trade" and the entire income arising from the activity could be taxed under the head "profit and gains from business".
In order to minimize and postpone the tax burden the following steps should be adopted by the individual:
 - a) The immovable property in question hitherto held as investment asset (capital asset) and recorded as such by him in his books of account should be converted and treated by him as a business asset i.e. as stock-in-trade in his books of accounts and financial records. This act of conversion and treatment as stock-in-trade should be substantiated/ supported by a self declaratory affidavit duly notarised.
 - b) The market value of the immovable property on the date of conversion as above should be determined at the maximum value possible duly supported by a valuation certificate of an approved valuer.
 - c) The taxation in the case of individual would arise on the development as and when and in the year in which the immovable property held as stock-in-trade is sold or otherwise transferred under the explicit provisions under Section 45 (2) of the Income Tax Act. As per the provisions of the said Section the difference between the

market value of the immovable property less indexed cost would be taxed under the head “Capital Gains” and the difference between the sale price and the indexed cost would be taxed under the head “Profits and Gains from Business and Profession” and such tax incidence would arise only in the year of sale or transfer of such stock-in-trade.

It is pertinent to note that the Kolkata Tribunal in the case of **Octavius Steel and Company limited Vs. ACIT(2002) 83 ITD 87** has held that Section 45(2) supersedes all the provisions including Section 45(1) and provides for charging of Capital Gains in the year when such converted stock in trade is sold or otherwise transferred.

In the case where the individual intends to enter an agreement for joint development with the Builder on an area sharing or an agreement for revenue sharing, such an agreement should be entered into by the said individual only after the said immovable property is converted and treated as stock-in-trade in his books of accounts and financial statements. This would eliminate the applicability of the incidence of capital gains tax on the individual as on the date of entering the joint development agreement itself as has been held by a catena of decisions given below-

- iii. In the case of a Firm, LLP or company (the assessee) which intends to exploit the excess land owned by it and originally acquired for the purpose of present business operations and treated as fixed assets/ investments in the books, the said assessee should take the following steps before it intends to develop the said property on its own or through a developer

Apply for change in its Objects to include the object of real estate development

Apply for change of name to indicate real estate as one of its main objects

Change the disclosure of the immovable property to the extent being developed from Fixed Asset to Current Asset

Pass a Journal entry in the books of account with an explicit narration disclosing the conversion of the immovable property and its treatment as stock-in-trade in the books of account.

Once the capital asset gets converted and treated as stock-in-trade in the hands of the individual, firm, LLP, Company as the case may be, care should be taken to insert the following clauses in the agreement for joint development or revenue share as the case may be –

- a) The fact of the immovable property being held as a business asset and disclosed as stock-in-trade in the books of the owner.

- b) The fact that the legal ownership, domain and control continue to vest in the owner till such time it is transferred to the prospective buyers of apartments, villas etc in the project.
- c) The fact that the licence given to the developer to enter and commence the development is in the nature of a licence referred to under Section 52 of Indian Easements Act, 1882 and cannot be construed as a possession given by the Owner to the Developer in part performance of the agreement of the nature referred to under section 53A of the Transfer of Property Act, 1882
- d) The Development contemplated in the Agreement is not in the nature of a Partnership as contemplated either under the Indian Partnership Act, 1932, or under the Income Tax Act, 1961.
- e) The fact that the owner should be allowed uninterrupted and unhindered right to inspect the development without the prior permission of the developer during normal working hours.
- f) The Developer will be given the power to do all acts, deeds and things for the development of the property including the right to enter into agreements for sale and raise finances on the developers share in the development but his power to execute the deeds of sale in favour of the purchasers of the developers share can be invoked only after the Developer hands over the Owners Share in a habitable condition.

- iv. In such cases only the provisions of Section 2(47) (iv) read with Section 45(2) come into operation and there is no scope for invoking provisions of Section 2(47)(v) and (vi) or any reference being made to Section 53-A of the Transfer of Property Act 1882 through Section 2(47)(v). The profits and gains arising out of such conversion into stock-in-trade will be governed by the provisions of Section 45(2). This would mean that the capital gains arising to the Owners on the date of such conversion to stock-in-trade will get quantified at that stage itself but its chargeability to tax will arise only when sales or transfers otherwise of such stock-in-trade take place subsequently. It should be clearly noted that such subsequent sales or transfers otherwise will be of stock-in-trade only and provisions of Section 2(47) cannot be invoked for such subsequent sales or transfers of stock-in-trade.
- v. The profits and gains earned on subsequent sales affected by the Owners of their surplus flats / apartments (other than what are kept for their own use) will be taxed as business income only. In the normal course, these sales would have been made within a period of two (earlier three years) from the date of completion of the project

and they would have been subjected to tax as “short term capital gains” only and the tax incidence would have been the same on the Owners.

There are catena of judicial decisions which have held that there will be no transfer as on the date of entering into Development Agreement or as on date of handing over possession to the Developer in cases where the Owner was holding and treating the immovable property as stock in trade or on prior to the date of entering into the Development Agreement. The decisions to be noted in this regard are:

- **R Gopinath (HUF) v. ACIT (2010) 5 Taxmann.com ITA Nos. 29 & 30/MDS/2008 rendered by the ITAT Chennai 'A' Bench on 24th July, 2009 also reported in 133 TTJ (Chennai) 595.**
- **Ramesh Abaji Walavalkar v. Addln CIT 150 TTJ 725 Mum Trib. (D Bench)**
- **Vidyavihar Containers Ltd v. Dy. CIT (2011) 133 ITD 363 (Mum. Trib)**
- **DCIT vs Crest Hotels Ltd (2001) 78 ITD 231 (Chennai Bench).**
- **Fardeen Khan Vs ACIT 11(1) Mumbai- ITA No 1588/1589 of 2013 (ITAT F Bench Mumbai) rendered on 25-2-2015 and reported in 169 TTJ 398 and in (2015) 58 taxmann.com 186.**
- **Dheeraj Amin Propreitor J V Builders Vs ACIT Circle 2(1) Mangalore ITAT NO 1709/Bang/ 2013 rendered on 30-6-2015.**

In a related decision in the case of **ACIT Central Circle-8 (Hyd) vs. Medravathi Agro Farms (P) Ltd (2015) 63 taxmann.com 274 (Hyd-Trib"B" Bench)** rendered on 22/05/2015, it has been held that the transfer of land to the Developer or his nominees related to the Developer's share as per Joint Development Agreement will be taxed under the head "Capital Gains", while super built area along with the undivided share of land retained by the Owner would be taxed under the provisions of Section 45(2) i.e., by the presumption that the Owner has converted the capital asset into "Stock-in-Trade" on the date of entering into the Joint Development Agreement .Consequently, it has been held that the Capital Gains and business income would be chargeable to tax in the hands of the assessee company in a pro-rata basis as and when the built-up area is sold along with the proportionate share of land . While rendering this decision, the Tribunal has relied on the decision of **ACIT vs. Hill Country Properties Ltd (2015) 57 taxmann.com 400 (Hyd).**

F. TRANSFER TAKES PLACE ONLY WHEN THE BUILDER/DEVELOPER TAKES POSSESSION OF THE IMMOVABLE PROPERTY PURSUANT TO ENTERING INTO THE DEVELOPMENT AGREEMENT

It is to be noted that transfer u/s 2(47)(v) of the Income Tax Act, 1961 refers to any transaction involving the allowing of the possession of any immovable property to be taken or retained in part performance of a contract of the nature referred to in Section 53A of the Transfer of Property Act, 1882. In other words, for Section 2(47)(v) to be invoked, the transaction in question has to first fall under the rigours of the provisions of Section 53A of the Transfer of Property Act, 1882. On a reading of the provisions of Section 53A of the Transfer of Property Act, 1882 one of the essential conditions to invoke the provision of the said Section is that the transferee should have performed or be willing to perform his part of the contract. Based on the reading of the said Section, there have been several conditions rendered by Judicial Authorities which have held that "Transfer" will take place only when the Builder actually takes possession of the Schedule Property by commencing construction on the same.

Some of the decisions which have upheld the above analogy are detailed below:

The **Hyderabad Tribunal in case of Fibars Infratech Pvt. Ltd vs. ITO Ward 1(2) Hyderabad (ITAT Hyderabad), ITA. No. 477/Hyd/2013**, rendered on 03.01.2014 has also held that handing over **possession** of the property is only one of the conditions for invoking sec 53A of the Transfer of Property Act and is not the sole and isolated condition. The developer i.e. the transferee should be ready and willing to perform his obligation under the terms of the agreement and should have done some act, deed or thing to indicate the willingness. When there was a factual finding that the builder had not even of the Income Tax Act read with section 53 A of the Transfer of Property Act cannot be invoked. While rendering this decision the Tribunal has taken note of the decisions in the case of **Chaturbhuj Dwarkadas Kapadia, Jasbir Singh Sarkaria, Maya Shenoy and Dr T K Dayalu** referred to elsewhere in this article. The said decision has further been followed in the case of **ABVS Prakash Vs The Asst CIT Hyderabad Central Circle - 1 ITA No 462/Hyd/2013** rendered by the ITAT Hyderabad "B" Bench on 27-2-2014 in the case of **Binjusaria Properties (P) Ltd Vs ACIT (2014) 45 taxmann.com 115 (Hyd Trib)** also reported in (2014) Tax Pub (DT) 2438(Hyd "B" Trib) and in the case of **ACIT Central Circle 5 Hyderabad Vs R Srinivas Rao (2014) 50 taxmann.com 178 (Hyd Trib)** rendered on 28-8-2014 reported in 40 ITR (Trib) 266 (Hyd 'B' Trib).

Further, it is of significant interest to note that the Hyderabad- A Bench has in the case of **Ranjith Reddy Vs Dy CIT (Hyd) Circle 6(1) in ITA Nos. 290,292,336/Hyd/2012/rendered on 7/6/13 reported in 144 ITD 461 (Hyd "A" Trib)** held that there is no transfer as defined under Section (2)(47) (v) of the Income Tax Act read with Section 53 A of the Transfer of Property Act in the case of an agreement in the nature of Joint Development as on the date of signing the agreement, if there has been no progress or construction since the signing of the development agreement. While rendering this decision the Tribunal has clearly distinguished the decisions of **Charturbuj Dwarakadas Kapadia Vs CIT (2003) 260 ITR 491 (Bom)** and **Dr Maya Shenoy (2009)124 TTJ 692(Hyd) (Supra).**

The Chennai "D" Tribunal in the decision of Smt Sowcar Janaki v ITO (2013 27 ITR (Trib) 226 has also recognized the analogy of the Hyderabad Tribunal.

The Mumbai Tribunal has in the case of Dilip Anand Vazirani Vs ITO (2015) 57 taxmann.com 142 held that there will be no 'transfer' as on the date of the development agreement as the agreement only confers a licence to the builder to enter the property for construction but actual possession is not delivered to the builder till he commences construction. This decision is in line with the principles laid down by the decisions referred to in the previous para. **A similar view has been taken by the Mumbai Tribunal in the case of General Glass Co Private Limited v. Dy. CIT (2007) 108 TTJ 0854/ 2007 14 SOT 0032 (Mum.)**

Where the Developer took possession of assessee's land and started development work, said transaction was to be treated as transfer of right in property covered under Section 2(47)(v).

-Bertha T Almeida v. Income Tax Officer (2015) 53 taxmann.com 522 (Bom)

The above decisions could be the life line on which the Owners of properties who have entered into Joint Development Agreements can depend upon to postpone the incidence of Capital Gains till the date on which the Developer enters the property to commence construction activity as per the terms of the Development agreement. These decisions will be of immense help to cases who wish to postpone the "Transfer" to a period after 01/04/2012 so as to get the benefit of the provisions of the Section 50D of the Income Tax Act, 1961.

G. TRANSFER DOES NOT TAKE PLACE EITHER IN THE YEAR OF ENTERING INTO DEVELOPMENT AGREEMENT OR IN THE YEAR OF COMMENCEMENT OF CONSTRUCTION BUT ONLY IN THE YEAR OF RECEIPT OF CONSIDERATION BY THE OWNER IN THE FORM OF OBTAINING POSSESSION OF THE OWNER'S SHARE OF SUPER BUILT UP AREA.

There are a few decisions which have held that the license given to a Builder/Developer is only a permissive possession given to him/it for the limited purpose of carrying out the development as a "licensee" and hence such possession cannot be deemed to be a possession given in part performance of a contract of the nature referred to in Section 53A of the Transfer of Property Act, 1882 so as to invoke the provisions of Section 2(47)(v) of the Income Tax Act, 1961.

CIT V G Saroja (2008), 301 ITR 124(Mad)- No registration or possession given-Taxable event does not happen till such time

CIT Vs Attam Prakash & Sons(Del HC) IT Reference Nos 250-251 Of 1988 – delivered on August 8, 2008-(2008) 175 Taxman 499 (Del)-Mere grant of permissive right to Builder does not amount to "Transfer".

CIT-I vs Naju Daru Deboo (2013) 38 taxmann.com 258(All), 218 Taxmann 473(All) rendered 16-9-2013- Capital gain as a result of a joint development agreement can arise only at the point of receipt of consideration by the Owner and not on the date of entering into the Joint Development Agreement.

It is interesting and relevant note that the **High Court of Bombay at Goa has in the case of CIT Karnataka (Central) Bangalore v Shri Sadia Shaikh (Tax Appeal No. 11 & 12 of 2013) rendered on 2nd December 2013 reported in (2014) 56(I) ITCL 147 (Bom HC)** has held that possession given to a developer in pursuance of a Development Agreement cannot be regarded as a transfer under section 2(47) of the Income Tax Act read with section 53A of the Transfer of Property Act. The court seems to have based its decision on the fact that the entire control of the property, the license to construct on the property and the occupation certificate was given only in the name of the owner of the property.

Vijaya Productions P Ltd Vs Addl CIT(2012) 14 ITR (Trib) 614(Chennai), (2012) 134 ITD 19(Chennai Trib)TM: 144 TTJ 1 (Chennai Trib)- Date of entering into the agreement cannot be regarded as the date of transfer where the consideration is paid to the developer by way of allotment of shares in a Joint Venture Company incorporated between the Land Owners and the Developers.

In a recent decision in the case of - **Sujauddin Kasimsab Sayyed v. ITO [2020] 114 taxmann.com 168 (Mum-Trib) ITAT Mumbai Bench 'G'** it has been held that Immovable Property is considered to be transferred on the date of execution of registered document and not on the date of delivery of possession.

Further the Apex Court has in the case of **M/s. Seshasayee Steels P. Ltd v. ACIT, Company Circle VI (2), Chennai (SC) Civil Appeal No.9209 of 2019 rendered on 04/12/2019** held that handing over possession to the transferee does not amount to handing over control of land – Section 53 A is a legal concept, - transfer does not take place till the legal control is handed over. This decision can be used for buttressing the view that there can be no transfer of the Developers Share of land till the date of actual execution of the Deed of Conveyance in favour of the Developer and/or his nominees.

H. CONSIDERATION FOR THE PURPOSE OF TRANSFER

Having determined the point of incidence of tax on the Land Owner who has entered into Development Agreement the incidental issue to be discussed and concluded is the value to be deemed as "Consideration" received/accrued by the Land Owner for transfer of the Developer's portion of divided/undivided share of land, for the purpose of computation of capital gains for the Land Owner. In this regard there are two methods which could be taken as the most likely and prudent methods to arrive at the deemed value of consideration.

One of the methods is to be adopt the cost of construction of the Owners Share which is basically the replacement value of the land to be transferred by the Owner to the Developer and/or his/its nominees. This is duly supported in the following cases-

The Bangalore ITAT "A" Bench has in the case of ITO v/s M.S Nagaraj ITA No. 676/Bang/2011 vide its judgement rendered on 01.12.2014 reported in 52 taxmann.com 511 confirmed the analogy of the decisions in the case of Dr. T.K Dayalu and Ved Prakash Rakhra (Supra), by holding that the "transfer" takes place on the date of entering into Joint Development and the consideration for the purpose of transfer is the cost of construction to be incurred by the developer on the Owner share of super built up area. It is important to note that this judgement all though rendered after the provisions of Section 50D came into force relates to an assessment year which is prior to the year in which Section 50D was introduced.

It is relevant to note the High Court of Karnataka has in the case of **CIT Mysore Vs Khivraj Motors (2015) 62 taxmann.com 305 rendered on July 17th 2015** held that the

cost of construction incurred by the Developer on the sale of Super Built area of the Land Owner in a joint development is to be reckoned as per the value agreed to between the Developer and the Owner and not as per the project cost incurred by the Developer which could include many expenses which are not directly related to the construction activity.

The above analogy has also found judicial benediction in the following cases-

- Smt. Pratima Reddy vs. ITO, ward-6(4) (2012) 25 Taxmann.com 264 (Hyd)
- CIT v. Vasavi Pratap Chand and Sidharth P Chand (2017) 398 ITR 316 (Delhi)
- Udai Hospitals Pvt Ltd vs ITO. Ward 17(3), Hyd, (ITAT "B" Bench) ITA No. 1755/Hyd/2017 rendered on 28/09/2018
- Atluri Usha Rani vs Asst CIT - ITA Nos 1379 and 1544/Hyd/2016 rendered on 20/12/2017.
- CIT and Another vs Ved Prakash Rakhra(2015) 370 ITR 762 (Kar)- Exchange Value specified in the development agreement to be considered as deemed value of consideration and not the actual cost incurred by the Developer.
- P Madhusudhan Vs ACIT (2019) 419 ITR 194 (Mad)

The other method is adopting the value as determined under Section 50D of the Income tax Act, 1961 as the deemed value of consideration of the Owner for transfer of the land to the Developer and/or his/its nominees pertaining to the Developer's share. This method can be adopted for all Development Agreements entered into after 01/04/2012 or in such cases where the Development Agreement has been entered into earlier than the said date but in which cases the Builder/Developer has actually commenced construction after 01/04/2012.

In accordance with the provisions of this Section the deemed value of consideration to the Owner for transfer of the Developer's share of right, title and interest in land shall be based on the market value of the land as on the date of transfer. The option to adopt this method has found judicial benediction in the following cases:

B V Narayana Reddy v. Asst CIT (2015) TaxPub (DT) 4553 (Hyd 'B' - Trib) - TS- 5405-ITAT-2016(Hyd Trib)

ACIT vs M/s Shankar Vittal Motor Co. Ltd. ITA No.35/Bang/2015 rendered on 18/03/2016.

It is also to be noted that the CBDT had issued a Circular F.No.225/58/2016/ITA.II dated 29/02/2016 under which was regarding the payment of tax on Joint

Development Agreement under the Income Tax Act, 1961. In Para 3 of the said Circular, it is clearly stated that the landowner is liable to pay tax on the value of land in the year Joint Development agreement was entered into. This Circular gives a clear indication that Assessee can adopt valuation method as per Section 50D to offer capital gain arising from the transfer of Developer's share in land. (Circular is enclosed as Annexure-I)

I. IMPLICATION OF SECTION 45(5A)

Section 45(5A) was introduced by the Finance Act 2017 and applies to Development Agreement entered into on or after 01-04-2017. This Section was introduced to give relief to the landowners on the incidence of Capital Gain Tax which was arising on them on the date of signing the development agreement, which the revenue was insisting upon based on a catena of decisions mentioned elsewhere in the article.

However, even though objective of the Section was to mitigate the hardship of the land owner from the payment of capital gain tax even before he received the consideration in terms of his share of super built-up area, the Section may not achieve the desired result from the following reasons: -

- (i) The Section is only applies to Individual/HUF who is an owner of the Capital Asset which is subject matter of Development. Therefore, if the owner of the Capital Asset i.e., Immovable Property is owned by a Firm/AOP/LLP/Company, the said section would have no application. Consequently, where any of these entity entered into Development Agreement for development of immovable property owned by it and treated it is a fixed asset/investment in its books and Capital Asset for Income Tax purpose, such entities can be exposed to the levy of capital gain tax on the date of execution of development agreement or on the date of handing over possession to the developer to carry out the development activity, based on the analogy rendered by various decisions mentioned elsewhere in the article.
- (ii) A careful reading of the provision would indicate that though the charge of Capital Gain is postponed to the year in which the project is complete as manifested by the issue of a completion certificate by the Competent Authority, the transfer of the Developer's share in land occurs on the date of executing the "Specified Agreement". In other words, the provisions of the Section only fortifies the view taken by the various courts that the transfer of owner's share of land to the developer and/or nominees occurs at the point of execution of the development agreement.

- (iii) The consideration which is deemed as the full value of consideration for the purpose of transfer is the “Stamp duty value” (guideline value) of the land or building received by the land owner as his share plus non-refundable deposit if any. This would create a higher tax incidence as the alternate method of choosing the guideline value of the land which is being transferred as per the Provision of Section 50D cannot be adopted henceforth by the landowners who are Individual/HUF. Instead, they now have to adopt the guideline value of the land/building as the case may be received on return as on the date of issue of completion certificate which could be higher.
- (iv) The Section applies only to development agreement in the nature of area sharing agreement and not in the nature of revenue sharing agreement, as can be discerned from the definition of term “Specified Agreement” as defined in explanation (ii) of the Section 45(5A).
- (v) **The provisions of the Section have been held to be prospective in the case “Adinarayana Reddy Kummata vs ACIT Circle-11(1), Hyderabad [2018] 91 taxmann.com 360 [Hyderabad-Trib.]** In effect, any Individual or HUF who wishes to take the advantage of the Provisions of this Section in cases where Development Agreement has been entered into before 01-04-2017 may not be eligible to do so.
- (vi) As the “ Transfer” takes place on the date of execution of the “ Specified Agreement”, care should be taken to ensure that if the Assessee wants to invest in bonds to claim deduction under Section 54EC or in House Property to claim deduction under Section 54/54F, the time stipulated in the said Sections would commence from the date of entering into the Specified Agreement”.
- (vii) The Developer has been mandated to deduct tax at source at 10% on landowner as per the provisions of Section 194-IC of the Income Tax Act, 1961. The said Section clearly refers to payment to a resident of any sum by way of consideration, not being a consideration in kind i.e., non-refundable deposit received by the land owner. Consequently, the landowner would have to carry forward the TDS to claim credit for the same in the year in which he is liable to pay Income Tax as per the Provisions of Section 45(5A) of the Income Tax Act,1961 , which in accordance of the Provisions of Section 199 r/w Rule 37BA of the Income Tax Rules.

J. APPLICABILITY OF SECTION 50C TO TRANSFER OF DEVELOPMENT RIGHTS

It has been held by the Mumbai Tribunal in the case of **Sri Akhatar Hussain Vs ITO ITA No 541 of 2010 and ITA No 706 of 2010 reported in (2011) 140 TTJ 413** that the provisions of Section 50C are applicable to transfer of Development Rights also as they fall within the deeming provisions of Section 2(47) relating to transfer. A similar ruling has been given by the **Mumbai Tribunal in DCIT vs Jai Trikanand Rao(2014) 149 ITD 112 (Mum J Trib)**, in the case of **Chiranjeev Lal Khanna v ITO(2011) 132 ITD 474, (2012) 144 TTJ 607 (Mum)** and in the case of **Arlette Rodriques vs ITO (2011) 39(II) ITCL 328**.

However, in a recent decision of ITO Vs Balkawade Sadanand Dhanaji (2015) 66 (II) ITCL 410 (Pune A Trib), the Tribunal has held that Section 50C will not apply to development rights but will apply only to sale of land or building.

Further in the decision in the case of M/s Voltas Ltd Vs ITO Ward 7(3)(4) (2016)74 taxmann.com 99 rendered on 16-9-2016, the Mumbai Tribunal has held that the provisions of Section 50 C will not apply to transfer of development rights in land as the wordings of Section 50C clearly indicate that the transfer should be of land and building or both and does not include rights therein.

This is further followed by a decision in the case of **-ITO vs. SBI Staff Vaibhav Co-op HSG Ltd. ITA No. 5324/Mum/2016** (arising out of ITA No. 75324/Mum/2016) rendered on 19th June 2019.

The law is therefore not clear on this aspect.

K. WHETHER THE INCOME FROM SALE OF SUPER BUILT-UP AREA ALONG WITH UDI IN LAND REPRESENTING THE OWNER'S SHARE CAN BE TAXED AS INCOME FROM BUSINESS HOLDING THAT IT IS AN ADVENTURE IN THE NATURE OF TRADE

The Revenue can take a view that where the Owner gets multiple units/apartments towards his share in the Project and further markets the same as an organised activity the income generated by the Owner by sale of units/apartments can be treated as "an adventure in nature of trade" by the Owner and consequently taxed as "Business income".

In this regard reference could be made to the decision of the Calcutta High Court in the case of **Rungta Properties (P.) Ltd vs Pr.CIT (2017) reported in 83 taxmann.com 106** and

the Karnataka High Court in the case of M.V. Chandrashekar vs Dy.CIT (2004) reported in 91 ITD 543, wherein it has been held that the income generated by the Land Owner/s from sale of his share of units/apartments will have to be taxed as income from “Capital Gain”.

L. TREATMENT OF THE TRANSACTION BETWEEN THE LAND OWNER AND THE DEVELOPER AS AN ASSOCIATION OF PERSONS(AOP)

The Revenue can take a view that the development of the property by the Developer on the specific permission/license granted by the Land Owner and sharing of the super built up area between the Land Owner and the Developer, is a joint activity undertaken by both the parties for sharing the profits from the Project and consequently they can regard the arrangement between the parties as an Association of Persons and tax the profits derived from the Project accordingly.

In this regard it is pertinent to state that for an arrangement between the parties to be regarded as an Association of Persons, both the parties should be responsible for sharing all the risks and rewards relating to and arising out of development.

It is of relevance to note that while the entire responsibility and liability towards defect in title of the immovable property which is subject to development is on the Land Owner, the entire responsibility and liability towards construction and related activities is on the Developer. In fact, there is a clear indemnity Clause in the Development Agreement wherein, the Land Owner and the Developer indemnify each other with regard to the responsibility and liability as mentioned above. As the liability attached to their respective rights, responsibilities and obligations are clearly distinct and defined, the arrangement between them, cannot be held as an “Association of Persons”.

There are catena of decisions which have held that the development of a property under a Joint Development Method does not constitute an Association of Persons between the Owner and the Developer and the same are listed below:

- Faquir Chand Gulati vs Uppal Agencies Pvt. Ltd. & Anr (2014) TaxCorp(LI) 2618 (SC)
- Hyosung Corporation, (2009) 314 ITR 343 (AAR)
- VAN OORD ACZ. BV, (2001) 248 ITR 399 (AAR)

While rendering the above decisions the Courts referred to the decisions of the Apex Court in the cases of:

- Indira Balkrishna (1960) 39 ITR 546 (SC)
- Murugesan and Bros as held in the case of (1973) 88 ITR 432 (SC),

which had laid down the law with respect to an “Association of Persons”.

M. REVENUE SHARING ARRANGEMENTS-TAX IMPLICATIONS AND OTHER ISSUES.

1. Nature of agreement, arrangement-

There is the emerging trend in the Real Estate Industry wherein the Land Owners and Developers enter into a Revenue Sharing Agreement/ Arrangement to share the proceeds arising from the development of immovable property belonging to the Land Owner. Under these agreement/ arrangements

- i. The Land Owner and Developer agree to share the "Distributable Revenue" in a specified percentage. The term "distributable revenue" is specifically defined in the development agreement apart from other terms and conditions.
- ii. Various terms such as “Gross Revenue”, “Distributable Revenue”, “Pass through Charges”, the mode and method of sharing the revenue etc, are defined in the agreement.
 - **“Gross Revenue”** shall mean the total revenue accruing and arising to the “Project” by way of receipts from Purchaser/s/Allottee/s in the “Project” including the basic sale price on consideration, “Pass Through Charges”, “Additional Charges”, “Floor Rise Charges”, “Premium Location Charges” and “Other Charges”.
 - **“Distributable Project Revenue”** shall mean and include the “Gross Revenue” accruing and arising to the “Project” by way of receipts from Purchaser/s/Allottee/s in the “Project” including the basic sale price on consideration, “Additional Charges”, “Floor Rise Charges”, “Premium Location Charges” and “Other Charges” other than “Pass Through Charges” but shall not include the marketing fee payable to the Developer, the cost of interest and compensation paid to the Purchaser/s/Allottee/s relating to project construction and development which shall be borne by the Developer only and the compensation paid to the Purchaser/s/Allottee/s on claims relating to title which shall be borne by the Owner only.
 - **“Pass Through Charges”** shall refer to all statutory charges, fees and expenses, such as club membership fees and charges, external electrification charges, Power backup charges, , payments / contributions received from the customers towards electricity, water, sewerage deposit and other connection related charges, maintenance security deposit, advance maintenance charges, Reticulated Gas connection and related charges and deposits, association deposit, GST and any

future taxes levied by any Governmental Authority, stamp duty, registration charges, and all such other similar statutory charges, fees and costs which would be collected / recovered from the customers in relation to the "Saleable Area" as a contribution from the customers and for the onward transfer / deposit to the concerned Government Authority or "Association of Allottees" in the "Project".

- iii. The Land Owner and the Developer join together in a tripartite agreement with the ultimate purchaser of the apartment wherein the Land Owner agrees to convey undivided right, title and interest in land to and in favour of the prospective purchaser of apartments and the Developer agrees to convey the specified super built up area being constructed on the land in favour of ultimate purchaser of the apartments.
- iv. A General Power of Attorney is executed by the Land Owners in favour of the Developer giving him the powers to do all acts, deeds and things in pursuance to the Revenue Sharing Agreement/Arrangement including the power to sell the UDI in land in favour of the prospective purchasers.
- v. The agreement could be worded in a manner to indicate that the revenue share accruing to the Land Owner is in essence only for the transfer of the undivided share of right, title and interest in land and the revenue share of the Developer is for transfer of specified super built up area.
- vi. The insurable interest of the super built up area being constructed on the land would be on the Developer during the period of construction and till the date of its transfer.
- vii. The legal ownership, domain and control of the land remains vested with the Land Owner and no portion of it will be transferred to the Developer or his nominees as the case maybe.
- viii. There is no allocated area designated as Owner's share and Developer's share as the case maybe.

If the agreement is drafted keeping the above principles in mind, it can be ensured that the Land Owner pays tax as " Business Profits" only at the point of transfer of risks and rewards of ownership in favour of the transferees i.e., the purchaser of apartments, which event would occur either at the point of execution of Sale Deed or handing over possession of the apartment whichever is earlier.

Further by entering into Revenue Sharing Agreement/Arrangement the possibility of levy of GST on the Owner's share of revenue does not arise.

Whereas, in the case of Joint Development Agreement based on area share, there is a need for the Developer to levy GST on the Owner's share of super built up area as mandated by circulars issued by the relevant authorities.

2. Issues arising out of Revenue Sharing Agreement

i. Point of incidence of tax on the owners.

As the revenue share derive from the Land Owners is essentially and in essence for the transfer of 100% undivided share of right, title and interest in the land in favour of the ultimate purchasers of Apartments/units in the Project, the revenues shall be recognized by the Land Owners only at the point of transfer of risks and rewards of ownership of divided/undivided share of land to the purchasers of units i.e., at the point of conveyance or possession whichever is earlier.

ii. Point of incidence of tax on the Developers who are not contractors

It is been held in the following cases where the Developer is outsourced the entire construction activity to the contractor, revenue can be recognized by the Developer only at the point of transfer risks and rewards of ownership to the ultimate purchasers of the units in the Project.

- S N Builders and Developers Vs ACIT 4(1) Bangalore ITA No 487/Bang/2013 rendered on 11-4-2014.
- Prestige Estate Projects Ltd V DCIT ITA 218/Bang/2009 (ITAT Bangalore)
- CIT Vs Rema Country Holdings Pvt Ltd ITA No 1041 and 1042/2006 order dated 29-9-2011 (Kar HC)
- ACIT v Layer Exports (P) Ltd (2017) 53 TR 416 (Mumbai- Trib)
- Shivalik Buildwell (P) Ltd v CIT (2013) 40 taxman.com 219 (Gujarat)
- Paras Buildtech India (P) Ltd v CIT (2016) 382 ITR 630 (Delhi)
- CIT v Excel Industries Ltd (2013) 358 ITR 295 (SC)

iii. Applicability of Section 50 D

As in the case of Revenue Sharing Agreement, there is no “transfer” contemplated between the Owner and the Developer as there is no defined “Owners share” and “ Developers Share”, the provisions of Section 50D will not be applicable.

iv. Applicability of Section 45(5A)

The term “specified agreement” defined in the explanation (ii) under the Section 45(5A) applies to an area sharing agreement and not to a revenue sharing arrangement.

v. Tax Deducted at Source on the Land Owner and the Developer by end customers/purchasers.

In the case of Revenue Sharing Agreement, it is a normal practice for the entire consideration received from the prospective purchasers of the units including the pass-through charges to be deposited in one common bank account normally opened in the name of the Project. The share of the revenue of the Land Owner Developer will then be transferred to respective bank accounts of the Land Owner and the developer usually opened in the same bank. The Revenue to be transferred to the account of the Developer includes all the pass through charges.

Due to above mechanism of receipt of monies and distribution, there has been a practice of allowing the buyers of units to deduct tax at source under Section 194 IA only in the name of the Developer. The Developer in turn deducts tax at source at the rates specified under Section 194IA on the Land Owner to the extent of his/its distributable share of revenue.

This practice in opinion of the Author is not correct as it indicates the Developer is a transferee for the entire Owners share of revenue whereas the actual transferees are the numerous end buyers of its units. It would therefore be appropriate to intimate the buyers to deduct tax at source both in the name of the Owner and the Developer to the extent of their respective revenue share.

However, the recent mandate by the RERA Authorities in certain states that there can be only one bank account for a Project can create several practical issues.

L. ALTERNATE STRUCTURES TO BE EVOLVED

Taking into consideration the various factors including the levy of stamp duty on Developments agreements and the Power of Attorney incidental thereto, the ineligibility for set off of stamp duty on subsequent sales to the ultimate customers, the various judicial decisions referred to above which seek to pre-pone the incidence of tax on the Land Owner even before he receives the consideration for development of land, the incidence of GST on the Owners Share of Super Built Area being constructed by the Developers in lieu of the undivided/divided share of land being conveyed to the

Developers and/or their nominees, the incidence of GST on the supply of development rights by the Land Owner to the Developers etc , it is for professionals like us to put on the thinking caps and evolve a suitable structure which could minimise the impact of the above.

I am detailing below a few options which could be explored in the case of potential Joint Development/s.

I. Formation of a partnership firm between the Land Owner and a Developer

The above methodology could be adopted ideally in cases where a development is conceptualised on a revenue sharing model that is where there is no identifiable area between the Land Owners and Developer post development and where the agreement is to share the gross revenues other than taxes and deposits between the land Owner and Developer in an agreed ratio.

This scheme is conceptualised as follows:

- i. The land Owner contributes the immovable property into a partnership firm at a value which is equivalent to the guideline value (Circle Rate) of the property. On such value being recorded in the books of the firm there would be an incidence of Capital Gain tax on the land Owner to the extent of difference between the value recorded in the books of the firm and the indexed cost. As the property will be recorded at an enhanced value in the books of the firm, the same value will be recorded as an expenditure of the firm as and when the property is sold or otherwise transferred. The sharing of the capital gains tax and the benefit derived from the differential tax benefit derived from the firm, will be shared between the Owner and Developer as agreed upon.
- ii. The contribution of immovable property into the firm would be in accordance with Section 14 of the Indian Partnership Act 1932 and would therefore be recognised and treated from thereon as the firm's property.

It is to be noted that the act of contribution of an immovable property in to the firm will entail payment of stamp duty at the rate applicable to conveyance in the State of West Bengal. Further it will also entail the payment of registration fee of 1% as prescribed under the table of registration fees issued under Section 78 of the Registration Act, 1908 and register the property in the favour of the firm so as to enable an entry in Book 1 maintained by the Sub-Registrars under the

Registration Act, 1908. This would help in securing a better title to the property and in getting the Khata of the property transferred in the name of the firm.

- iii. The Developer should also become a partner in the said firm by making his initial financial contribution as agreed upon.
- iv. It is to be clearly provided in the partnership deed that the entire cost of construction of the development would be borne by the Developer.

Further the clause on profit sharing would be worded in a manner so as to ensure that the land Owner would be entitled to draw as profits, a fixed percentage of the gross revenue exclusive of GST and deposits less the proportionate Income Tax to be borne by him. Similarly, it would be provided that the Developer would be entitled to draw as profits, a fixed percentage of the gross revenue less the construction cost less the proportionate Income Tax payable borne by him excluding GST and deposits.

- v. The Developer would be giving an unbridled right as a partner of the firm to all acts, deeds and things necessary for the purpose of development as he would have done as a power of attorney holder under conventional development agreement.
- vi. The firm would have a common bank account referred to as the principal bank account for the collection of revenue i.e. the instalments towards consideration from the buyers including moneys towards taxes and deposits.

The share of revenues attributed to the Owner excluding the amounts received towards GST, Deposits and other pass through charges etc will be transferred understanding instructions to the bank to another bank account opened in the name of the firm to be exclusively operated by the owners from which the Owner would be entitled to draw his share of revenue/ profits as the case may above.

The Developer would either continue to spend for the development of the property from the said principal bank account or transfer his share of revenues to another designated bank account opened in the name of the firm from which the entire construction cost and other relevant expenses would be defrayed.

The GST and deposits collected from time to time i.e pass through charges would be left in the principal bank account of the firm and paid to the respective statutory authorities and bodies as per time lines prescribed.

- vii. The Partnership deed would also have a specific indemnity clause between the partners indemnifying each other of possible ill effects on the firm in the event of their partnership share being attached or affected due to losses incurred by them in business/es other than that of the firm.
- viii. The clause on dissolution would be worded in a manner so as to ensure that the land reverts back to the partner who has originally contributed it as capital contribution on dissolution until a threshold limit of cost incurred on development is reached by the Developer. The rights on the land at various stages of development in the event of dissolution can be detailed in the partnership deed.
- ix. The firm would then convert and treat the immovable property introduced by the Owner which was a Capital Asset in his hands as capital contribution into the firm as mentioned above into stock in trade in its books. This event could be timed to be simultaneous with the approval of sanction plans, other permissions, clearances, etc obtained for the project.

This would ensure that the tax on the profits out of the development would get taxed as Capital Gains and Business income only at the point when such stock in trade is sold or otherwise transferred under the specific provisions of Section 45(2) of the Income Tax Act.

This would also be in line with the revenue recognition as mandated under AS 9 issued by Institute of Chartered Accountants of India.

It is to be noted that in the case of Developers developing housing projects on their own account as a commercial venture wherein the construction activity is outsourced to contractors, it has been held that the recognition of revenue as per the principles laid down in AS 9 issued by the ICAI is in order. Reference in this regard can be made to the following decisions-

Dy. CIT V Sudhir V Shetty (2014) 35 ITR (Trib) 115 (Mum "H" Tribunal)

S N Builders and Developers Vs ACIT 4(1) Bangalore ITA No 487/Bang/2013 rendered on 11-4-2014

Prestige Estate Projects Ltd V DCIT ITA 218/Bang/2009 (ITAT Bangalore)

CIT Vs Rema Country Holdings Pvt Ltd ITA No 1041 and 1042/2006 order dated 29-9-2011 (Kar HC)

Case referred- CIT Vs Hyundai Heavy Industries Company Ltd (2007) 161 Taxman 191 (SC)- assessee has a choice to select project completion or percentage completion method for recognising revenue.

Under the above scheme as there is no transfer or deemed transfer of immovable property by the Owner in favour of Developer during the period of development and as there is no necessity for a Power of Attorney to be given to the Developer as would have otherwise been done in a conventional development agreement, the ramifications arising out of the stamp duty applicable to development agreements and the adverse judicial tax decisions mentioned elsewhere in this article would be practically eliminated.

II) Formation of a Limited Liability Partnership between the Owner and the Developer

As a partnership suggested above could involve the effect of unlimited liability being foisted on the firm and possibly its other partners, in case the Owner and Developer do not have a credible knowledge of each other's background it would be preferable to form a Limited Liability Partnership as against a Partnership firm suggested above.

However, as a Limited Liability Partnership is different legal entity and although there is an enabling provision for a partner to contribute tangible, movable, immovable or intangible property or other benefit u/s 32(1) of the LLP Act 2008, it could be possible only through a registered conveyance thereby involving stamp duty and registration charges. It is significant to note that the stamp act of various states do not have a specific article dealing with the applicability of stamp duty on the immovable properties owned by the firm when the firm is converted to and registered as an LLP and in the absence of such article, it is anybody's guess as to what rate of stamp duty would become applicable when an immovable property is contributed by a partner into an LLP as his/its capital contribution. It should be examined as to whether an LLP would be treated as a firm under the Stamp Act and Rules of the States which do not have a specific article for this purpose.

The other aspects which could affect the scheme evolved as in the case of a Limited Liability Partnership suggested above would be as follows:

- i. Under the Limited Liability Partnership Act, the value of the property brought in as capital contribution by the partners to be recorded in the books of Limited Liability Partnership would be described under the Limited Liability Partnership Rules as specifically provided u/s 32(2) of the Limited Liability Partnership Act.

As per Rule 23 (2) of the Limited Liability Partnership Rules, 2009 the value of contribution of the immovable property would be as determined by a practicing Chartered Accountant/Cost Accountant/ Approved Valuer from the panel maintained by the Central Government. Consequently, there could be incidence of capital gains u/s 45(5) of the Income tax Act, 1961 in the initial stage itself. It is to be noted that the definition of "Firm" u/s 2(23) of the Income Tax Act includes a Limited Liability Partnership as defined in the Limited Liability Partnership Act, 2008 (6 of 2009) and definition of a "Partner" shall include a partner of a Limited Liability Partnership.

- ii. The other aspects mentioned in the case of a firm in Para I above would equally be applicable to a Limited Liability Partnership.
- iii. There could also be an impediment for immediate conversion of a firm into an LLP as although there is no stipulation in the LLP Act or LLP Rules, there is a mention in Form No 17 which is a part of the procedure for conversion of a firm to an LLP, that the firm should have been in existence for atleast one financial year and that a no objection certificate should be obtained from the Income Tax Authorities along with the application.

III) Developer to act as a Contractor

Under this method the land owner would hand over the responsibility of construction of the entire super built area to the builders through a construction contract. The Builder/ Developer would be performing his/its role as a contractor and not as a developer although such contractor would perform the same functions as that of a developer.

The agreement would state that the contractor would recover the fee due to him for construction by way of a right to sell a specified percentage of undivided share of land and super built area which will be referred to as "contractor's share".

The entire land would continue to be owned by the owners and the entire receipts including that of the contractor's share would be disclosed as sales revenue in the owner's hand. From the said revenue the owner will reduce the fee paid to the

contractor towards construction including the GST charged by him, which will be equal to the sale proceeds derived from transfer of the contractor's share. The contractor shall declare the contract receipts as his income and reduce the actual cost of construction incurred by him to arrive at his profit.

The GST from the buyers would be collected in the name of the owner and deposited to the respective authorities accordingly.

A Power of Attorney would be given to the contractor to do all acts, deeds and things as would normally have been done by a developer and such Power of Attorney would confer the status to the contractor as "an agent coupled with interest" as understood under Section 202 of the Indian Contract Act, so that the owner would not be able to revoke such Power of Attorney during the period of construction except for specific circumstances mentioned therein.

It is to be noted that as the owner would continue to hold the legal and possessory right on the property till it is ultimately transferred to the buyers, the revenue from such sales would be recognized only as and when transfer of property takes place.

In such an arrangement the Developer being a contractor will declare his/its revenue under the percentage of completion method while the Owner can declare his/its revenue as per the principles laid down in AS 9 issued by the ICAI. It is to be noted that even as per the Income Computation and Disclosure Standards III relating to construction contracts issued by the CBDT to be effective from 1-4-2015, the said standard applies only to the income for a construction contract of a contractor.

Conclusion:

This article attempts to bring about various issues pertaining to the Direct Tax implication on development of immovable property through the mechanism of Development Agreements under the Area Sharing and the Revenue Sharing Models.

This Article has not dealt with the impact of indirect taxes i.e., GST on transfer of development rights and works contract and the GST applicability on the end purchasers of units/apartments and has also not dealt with various aspects of RERA which are relevant to the aforesaid models of development

It is critical to understand that each case should be thoroughly analysed keeping in mind the objectives of the parties concerned and the plethora of taxes which could affect the transaction before the same is documented either as an Area Sharing Agreement or a Revenue Sharing Agreement.

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