Real estate transactions

Tax Implications

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Advocate
## Synopsis

### Tax Implications

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# Synopsis

## Joint Development Agreements

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## Synopsis

### Valuation

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LAND OWNER
INCOME
CHARACTERIZATION
Land owner: Income characterization

- If charged as LTCG, indexation of cost and concessional rate of tax under section 112 would apply. Section 50C/50D would apply.

- Further, deduction under section 54, 54EC and 54F would be available.

- If charged as short term capital gains, normal rate of tax would apply and no incentives are available.

- If charged as business income, normal rate of tax would apply and provisions of sections 54, 54EC, 54F and section 112 are not applicable.

- However, section 43CA would apply whereas section 50C and section 2(47) don’t apply.
Land owner: Income characterization

a) Board circulars:
   - Draft Instructions of CBDT (2006) 153 Taxman-St 9
   - CBDT Instruction No. 1827 dated 31.08.1989
   - CBDT Circular No. 4, dt. 15-6-2007

b) Case laws:
   - G. Venkata Swami Naidu & Co. v CIT (1959) 35 ITR 594
   - H. Mohammad & Co. v. CIT (1977) 177 ITR 637 Gu
   - Sarder Indra Singh & Sons v. CIT (1953) 24 ITR 415 SC
   - Karam Chand Thapars & Bros. V. CIT (1971) 83 ITR 899
Tests for determination – Courts

- Whether initial acquisition was with intention of dealing in the item, or with a view to finding an investment

  *Does transaction, since inception, appear to be impressed with character of a Commercial transaction entered into with a view to earn profit*

- Why, how & for what purpose sale was effected subsequently

- How assessee dealt with subject-matter of transaction during the time the asset was with the assessee

  *Has it been treated as stock-in-trade, or has it been shown in the books of account and balance sheet as an investment. This inquiry, though relevant, is not conclusive*
Tests for determination – Courts

- How assessee himself has returned income from such activities and how Department has dealt with same in the course of preceding and succeeding assessments.

  *This factor, though not conclusive, affords good & cogent evidence to judge nature of transaction and is relevant to be considered in absence of any satisfactory explanation.*

- Whether partnership deed or MA authorizes such an activity.

- The most important test, is as to the volume, frequency, continuity and regularity of transactions of purchase and sale of the goods concerned.

  *Where there is repetition and continuity, coupled with the magnitude of the transaction, bearing reasonable proportion to the strength of holding, then an inference can readily be drawn that the activity is in the nature of business.*
Single transaction – does it constitute a business?

- Yes as per
  - 250 ITR 127 Mad.
  - 100 ITR 706 SC [Sutlej cotton Mills]

- Not necessarily as per
  - 195 ITR 386 Bby.
  - 195 ITR 767 All.
  - 77 ITR 253 SC [Raja Bahadur Kamakya Narain Singh]
TIMING OF TAX
### Timing of Tax

**a)** Where held as a capital asset

- In the year of transfer
- Method of accounting is not relevant
- Transfer is as per section 2(47)
- Applicability of section 53A of TP Act
Timing of Tax

b) Where held as a business asset

- In the year of sale
- Method of accounting, cash/ accrual, will decide the year of tax
- Extended meaning of transfer as per section 2(47) is not applicable
Timing – Sec 2(47) of IT Act

(v) any transaction involving allowing of the possession of any immovable property to be taken/retained in part performance of a contract of the nature referred to in section 53A of the TP Act, 1882; or

(vi) any transaction (whether by way of becoming a member of, or acquiring shares in, a co-operative society, company or other AOP or by way of any agreement or any arrangement or in any other manner whatsoever) which has the effect of transferring, or enabling the enjoyment of, any immovable property.
Sec 2(47) – Circ 495 dt 22.09.87 Para 11

• The existing definition of "transfer" in s. 2(47) does not include transfer of certain rights accruing to a purchaser, by way of becoming a member of or acquiring shares in a co-op society, company, or AOP or by way of any agreement or any arrangement.

• Whereby such person acquires any right in any building which is either being constructed or which is to be constructed.

• Above transactions are not required to be registered under Registration Act, 1908.
Sec 2(47) – Circ 495 dt 22.09.87 Para 11

- Such arrangements confer privileges of ownership without transfer of title in the building and are a common mode of acquiring flats particularly in multi-storeyed constructions in big cities.

- Sec 2(47) does not cover cases where possession is allowed to be taken/retained in part performance of a contract as referred to in s. 53A of TP Act

- New sub-clss. (v) & (vi) are inserted to prevent avoidance of capital gains liability by recourse to transfer of rights in the manner referred to above.
The newly inserted sub-cl. (vi) of s. 2(47) has brought into the ambit of "transfer", the practice of enjoyment of property rights through what is commonly known as Power of Attorney arrangements.

The practice in such cases is adopted normally where transfer of ownership is legally not permitted. A person holding the power of attorney is authorised the powers of owner, including that of making construction. The legal ownership in such cases continues to be with the transferor.
Sec 53A of TP Act

• 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
Sec 53A of TP Act

- 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,
Sec 53A of TP Act

• 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 therefor by the law for the time being in force,
Sec 53A of TP Act

• 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 the 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.
Sec 53A of TP Act – Important amendment

- Amendment carried out by the Registration and Other Laws (Amendment) Act, 2001

- With effect from 24.9.2001

- The words “the contract, though required to be registered, has not been registered” have been omitted

- Effect of amendment is that sec 53A does not come to the rescue of transferee in case a contract entered into on or after 24.09.2001 has not been registered
Section 17(1A) of the Registration Act, 1908

- The documents containing contracts to transfer for consideration, any immovable property for the purpose of section 53A of TP Act, 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, then, they shall have no effect for the purposes of the said section 53A.
Impact on Sec 2(47) (v)

- Impact of amendment to sec 17(1A) of IRA and sec 53A of TPA on section 2(47) of IT Act

- Section 2 (47) (v) of the Income-tax Act comes to the aid of the Department only if the conditions of section 53A of the Transfer of Property Act are satisfied as per CIT v. G. Saroja [2008] 301 ITR 124 (Mad) HC

- No impact as per Shri Satnam Singh Kainth vs ITO & Shri Sureshchandra Agarwal Vs ITO 2011-TIOL-662-ITAT-MUM
Date of agreement – is date of transfer?

- Agreement date is date of transfer - Chaturbhuj Dwarakadas Kapadia v. CIT (2003)260 ITR 491 (Bom.)

- In fact, the limited power of attorney may not be actually given, but once under the agreement a limited power of attorney is intended to be given to the developer to deal with the property, then the date of the contract would be the relevant date to decide the date of transfer under section 2(47)(v) and, in which event, the question of substantial performance of the contract thereafter does not arise.

- If the contract, read as a whole, indicates passing of or transferring of complete control over the property in favour of the developer, then the date of the contract would be relevant to decide the year of chargeability.
Date of agreement – is date of transfer?

- Agreement date is date of transfer - [Potla Nageswara Rao vs. DCIT 365 ITR 249 AP](#)

- Mere accrual of the consideration, to be received in the subsequent years does not defer the taxability of the capital gains.
Date of agreement – is date of transfer?

- Agreement date is not relevant as per

  - CIT v. Geetadevi Pasari [2009] 17 DTR 280 Bby
  - Dr. Arvind S. Phadke vs. ACIT 46 taxmann.com 335 (Pune)
  - CIT vs. Shakuntala Rajeshwar (1986) 160 ITR 840 (Delhi): Where an agreement was entered into for development and construction of a multistoried building, 1/4th interest of each of the transferors was transferred in 4 successive years by executing 4 separate deeds, “capital gains did not accrue on the execution of the first deed in the first year but accrued only proportionately in 4 years on the execution of the several deeds.

  - In CIT v. K. Jeelani Basha (2002) 256 ITR 282 (Mad.), it was held that transaction could be considered for the purpose of calculation of capital gains in parts

  - Execution of sale deed but sale to be effective upon satisfaction of certain condition: Agreement date is not relevant as per Smt. Raj Rani Devi Rama v. CIT [1993] 201 ITR 1032 Patna
Date of agreement – is date of transfer?

- Contra

Delivery of only part possession of the property: Even then, it comes within the ambit of Sec 53A of TP Act, and as the transaction is in relation to one property which is indivisible, the entire capital gains is exigible to tax in the year in which first part possession is handed over.

*ICI India Ltd. V. DCIT (2002) 80 ITD 58 (Calcutta).*
Possession under 2(47)(v)

- **Ajay Kumar Shah Jagati v. CIT** [2008] 168 Taxman 53 (SC) In order that the case would fall under the extended meaning of the word ‘transfer’, possession is essential element to be considered. That is the crux of the matter.
Possession under 2(47)(v)

- Possession as contemplated in cl. (v) need not necessarily be sole and exclusive possession, so long as the transferee is enabled to exercise general control over the property and to make use of it for the intended purpose. Fact that assessee owner has also the right to enter the property to oversee development work or to ensure performance of terms of the agreement; did not restrict rights of the developer or did not introduce any incompatibility. In this case, there is concurrent possession of both the parties, even then cl. (v) has its full role to play. As per Taher Alimohammed Poonawala v. ACIT [2009] 124 TTJ (Pune) 387

- It was so held in Jasbir Singh Sarkaria, In re [2007] 294 ITR 196 (AAR)
Possession under 2(47)(v)

- Possession v. License (permissive occupation): No right is created through a license as per Ramnord Research Laboratory P. Ltd. v. WTO [2008] 305 ITR 299 (Bom) HC

- A license to the developer to enter upon the land and to do certain preliminary work such as survey, setting up of site/sales office and make necessary arrangements required for future construction and marketing does not amount to possession as per Jasbir Singh Sarkaria, In re [2007] 294 ITR 196 (AAR)
Possession under 2(47)(v) - 294 ITR 196 (AAR)

• The actual date of taking physical possession or the instances of possessory acts exercised is not very relevant. It is enough if the transferee has, by virtue of that transaction, a right to enter upon and exercise acts of possession effectively pursuant to the covenants in the contract. That tantamounts to legal possession.

• Viewed in the light of the above meanings assigned to the two words “transaction” and “involving”, execution of the irrevocable GPA as a part of covenant of transfer agreement is a transaction under which possession is allowed to be taken by the transferee.

• Allowing the transferee to enter into possession of the land and to have general control and management of the property is an integral part of that GPA and as a result of such transaction possessory rights were conferred on the developer. It was an act done in part performance of the contract.
Willingness… Mulla’s views

• Willingness in the context of s. 53A of the Act has to be absolute and unconditional.

• If willingness is studded with a condition, it is in fact no more than an offer and cannot be termed as willingness. When the vendee company expresses its willingness to pay the amount, provided the (vendor) clears his income tax arrears, there is no complete willingness but a conditional willingness or partial willingness which is not sufficient...

In judging the willingness to perform, the Court must consider the obligations of the parties and the sequence in which these are to be performed....”

[“Mulla – The Transfer of Property Act” (9th Edn.)]
“The transferee has performed or is willing to perform his part of the contract”

- To ascertain the above, one must not put stop at one event but willingness is to be judged by the series of actions of the transferee.

- Vide a collaboration agreement, the transferees survey the land and to attract purchases put hoardings plus sales-office and carry out site development work. Landscaping, sales promotion, execution of construction and completion project are all incidental to demonstrate willingness of the transferee.

- On one hand, the power of attorney grants bundle of possessory rights to the developer simultaneously on the other hand transferee’s gesture of payment of consideration coupled with development work can be said to be a positive step towards willingness to fulfil the commitment.

Taher Alimohammed Poonawala v. ACIT [2009] 124 TTJ (Pune) 387
“The transferee has performed or is willing 
to perform his part of the contract”

- Section 53A would be triggered only if the transferee “has 
  performed” or is unconditionally willing and ready to perform his 
  part of the contract.

- In other words, if an agreement provides that the transferee will not 
  do certain act specified in the agreement unless he fulfills certain 
  conditions mentioned therein, it could not be assumed that the 
  transferee is willing to perform the remaining part of the contract 
  unconditionally.

- When the condition was to pay full and final consideration before 
  carrying out the development activity, and the transferee developer 
  did not pay the complete consideration and the possession 
  envisaged in the agreement is a conditional possession, it could not 
  be said that the development agreement of such type would be an 
  agreement which is envisaged to trigger the operation of section 
  53A.

Dr. Arvind S. Phadke vs. ACIT 46 taxmann.com 335 (Pune)
“The transferee has performed or is willing to perform his part of the contract”

- Property is in possession of a sister concern of the buyer which is not the same thing as in the possession of the buyer.

- Sister concern has compensated the seller for having occupied the property, under licence, beyond the time permissible under the lease and licence agreement.

- The buyer is not performing his part of the contract inasmuch as there have been delays in payments on instalments and there are disputes on interest charges in respect of the delay. The last payment of Rs 35 lakhs which should have been made on 30th June 2001 was not made till 25th October 2002. On these facts, the transferee cannot be even said to be, in June 2001, willing to perform his part of the contract. Of course, the transferee was not even in possession of the property either, but even if we leave that aside for a minute, the remaining conditions of Section 53 A are not satisfied either.

Cases on 2(47)(v) – Is a transfer

- **Smt. D. Kasturi v. CIT and another [2010] 323 ITR 40 (Mad) HC** For application of sec 53A, relevant consideration would be clauses in the agreement between parties to the agreement and their performance in terms of the agreement.

- Subsequent act of assessee in executing power of attorney and deeds executed by the power holder on basis of such power would not in any way alter the status of the parties to the agreement dt 29.03.1993, for applicability of section 53A as has been rightly held by the learned single judge.

- The assessee could no longer assert possessory rights against the firm to which possession was already given pursuant to the agreement and that too after receiving the full sale consideration.
Cases on 2(47)(v) – Is a transfer

- Where the transaction relating to transfer of leasehold rights of immovable property between the assessee and its group company was complete in the year 2001-02 itself in terms with the provisions of section 2(47)(v) of Income-tax Act, 1961 read with section 53A of the T.P. Act, 1882, the capital gain arising on the said transaction was chargeable in the said year itself as per Atlas Automotive Components Pvt. Ltd. v. ITO [2009] 313 ITR (AT) 398 (Mumbai)

- Fact that the assessee has allocated to the Builder 50 per cent of the building to be constructed and has also given the Builder the right to sell the Builder’s allocation to third parties proves that there is transfer as per CIT v. Ashok Kapur (HUF) [2007] 165 Taxman 569 (Delhi)
Cases on 2(47)(v) – Is a transfer

• Assessee having handed over possession of vacant land to the developer in terms of joint development agreement dt. 1\textsuperscript{st} March, 1995, transfer took place on that date and capital gains, if any, were chargeable in asst. yr. 1995-96 and not in 1998-99 in which assessee was handed over possession of constructed flats as per \textit{Vemanna Reddy (HUF) vs. ITO (2008) 114 TTJ (Bang) 246}

• Theatre property was transferred to the developer as per agreement dt. 8\textsuperscript{th} Aug., 1995 in view of the provisions of s. 2 (47) of the Act because the developer was given a right to demolish the existing structure of the cinema hall and carry out the development and construction work for the new commercial complex as per \textit{Mavany Brothers vs. DCIT [2007] 112 TTJ (Panaji) 82}
Cases on 2(47)(v) – Is a transfer

• Where with an intention to dispose of her property assessee entered into a memorandum of understanding with a builder, appointing him as sole and exclusive person to identify buyers and to complete related formalities for sale, and received certain amount from him as total sale consideration, that was a transaction by which assessee transferred property in question in manner prescribed in sub-clauses (v) and (vi) of section 2 (47), read with section 53A as per Ms.Rubab M.Kazerani v. JCIT (2004) 91 ITD 429 (Mum.)

• Intermittent dispute but agreement eventually honoured with higher consideration does not militate against operation of sec 2(47)(v) as per Taher Alimohammed Poonawala v. ACIT [2009] 124 TTJ (Pune) 387
Cases on 2(47)(v) – Not a transfer

• Mere grant of a permissive right to build on the plot of land would not amount to a transfer of capital asset as held in CIT v. Atam Prakash and Sons [2008] 175 Taxman 499 (Delhi). In the JV, it could be said that assessee has a stake and hence, it cannot be said that there is a transfer.

• Where payment of balance consideration within stipulated time is essence of the agreement of sale and such payments are not made in time by the transferee such a contract does not confer any right on the transferee as envisaged under s. 53A of TP Act, 1882, and provisions of s. 2(47)(v) cannot be applied in such a situation as per General Glass Co. (P) Ltd. vs. DCIT (2007) 108 TTJ (Mumbai) 854.
Cases on 2(47)(v) – Not a transfer

- Sec. 2 (47) (v) applies only in those cases where the transferor has performed or is willing to perform his part of the contract and the transferee has no part to perform in respect of the contract and has taken possession of the property or any part thereof as per ITO vs. Smt. Satyawati Devi Verma [2009] 123 TTJ (Del) 97

- Assessee never transferred 100% of right in land to AP Ltd. Only 56.8 per cent of the land was to be transferred to AP Ltd. and that too after completion of the development of the land. Agreements for sale between assessee and the purchasers clearly show that the assessee has also transferred proportionate undivided shares in the land to the purchasers as per The Statesman Ltd. vs. ACIT [2007] 112 TTJ (Kol) 593
Timing – Some interesting aspects

- Development agreement is executory contract and not to be construed as an agreement for sale simplicitor as per R. Vijayalakshmi V. Appu Hotels Ltd (2002) 257 ITR 4 (Mad)

- An agreement to sell is an executory contract as opposed to a contract of sale which is a executed contract (Mukul Dutta v. Indian Airline Corporation, AIR 1950 All 632).

- Apex Court in G.J. Fernandes v. I.T.C. Limited, reported in (1998) Judgments Today, has settled law to the effect that "that no authority nor even a Court can create a contract between the parties, when in reality no such contract exists"."
Timing – Some interesting aspects

- Subsequent cancellation of contract
  - Status of original assessment
  - Option available – sec 139(5), sec 264
  - The agreements finally ended in money transactions only and agreements had nothing to do with the transfer of possession of the property from vendor to vendee or from vendee to vendor: Hotel Harbour View [2009] 184 Taxman 42 Cochin ITAT:

- The perusal of tripartite agreement clearly shows that original agreement could not be acted upon for certain reasons and the same was cancelled ab initio and had to be treated as null and void: Dai-Ichi Karkaria Ltd (2008) 300 ITR (AT) 200 (Mumbai)

- Subsequent cancellation of contract followed by a new contract – status of past investment under sec 54 etc.
Since there was no separate stipulation in writing in the agreement, transfer of possession of the property could not be disassociated from the transfer of title in the property as per *ACIT v. Hotel Harbour View [2009] 184 Taxman 42 Cochin ITAT*.

The facts that other party had applied for electric connection, had obtained telephone connections, etc., did not go to decide the legal character of the transaction.
Timing – Some interesting aspects

• Value not mentioned in agreement – Does not matter as per CIT v. Ashok Kapur (HUF) [2007] 165 Taxman 569 (Delhi)

• Assessee not offering tax on transfer of possession but on various dates when the flats received were sold – Department taxing in the year of transfer of possession- Fate of tax already paid : DCIT v. Standard Fireworks P. Ltd. [2010] 4 ITR (Trib) 379 (Chennai)
Timing – Some interesting aspects

- Assessee owns a piece of land, obtains permission to develop it, converts the land into stock-in-trade and enters into JV agreement and starts construction work.

- AO holds that capital gains on the proportionate land pertaining to the Building which is completed and sold, are to be shown as income during the year.

- Assessee’s contention that the capital gains or profit of the whole project consisting of three buildings could be ascertained only on completion of the whole project and hence the capital gains pertaining to the proportionate land occupied by one building could not be taxed in this year but they are taxable in the year when construction of the flats in all the three buildings are completed in the subsequent year was not accepted in DCIT, Mumbai Vs Jehangir H C Jehangir 2010-TIOL-122-ITAT-MUM.
2(47)(vi)

- If not covered under sec 2(47)(v), a JDA may come under sec 2(47)(vi) on the basis of meaning of immovable property


- Since transaction resulted in dissolution of firm and partner getting rights over immovable property, same is transfer as per section 2(47)(vi) and assessee-firm was liable in terms of section 45(4) : Southern Tubes 306 ITR 216 Ker

- Once sold through power, subsequent registration does not attract tax liability : ITO v. Bansi Lal (2010) 124 ITD 400 (ASR.)
Conversion of capital asset into stock in trade

- Such conversion is deemed as transfer—Sec 2(47)(iv)

- FMV on the date of conversion shall be deemed to be full value consideration for the purpose of section 48

- However, capital gains will be charged to tax in the previous year in which such converted capital asset is sold or otherwise transferred

- The time limit for investment under section 54EC etc is however with reference to date of deemed transfer and not the date of actual sale. This position is mitigated by Circular No.791 of 2.6.2000
Conversion of capital asset into stock in trade

• FMV on conversion will be cost to business as per *CIT v. Bai Shirinbai K. Kooka* [1962] 46 ITR 86

• Need for such conversion
  - To overcome provisions of section 2(47)(v)/(vi)/50C
  - To possibly claim certain expenses particularly when the asset is held for not more than 36 months
  - To claim the set off of past unabsorbed business loss
Conversion of capital asset into stock in trade

- Section 45(1) deals with the profit and gain arising from the transfer of capital asset, whereas Section 45(2) deals with the profit or gain arising from the transfer by way of conversion of capital asset into stock-in-trade and shall be chargeable to income tax in previous year in which such stock-in-trade is sold or otherwise transferred.

- Time of chargeability of capital gain arising from the conversion of capital asset to stock-in-trade is the point when the stock-in-trade is sold or otherwise transferred, whereas the chargeability of capital gain u/s.45 from transfer of capital asset shall be in the previous year in which the transfer took place including the transfer as provided u/s.2(47).

- The sale / transfer of stock-in-trade cannot be equated with the transfer of capital asset.

Shri R Gopinath [HUF] Vs ACIT, 2009-TIOL-802-ITAT-MAD
Conversion of capital asset into stock in trade

- When such converted asset is sold, the sale index of year of sale not year of conversion has to be adopted as held by Kar HC in CIT & Anr. vs Rudra Industrial Commercial Corporation (HC) 20 Taxmann.Com 611 Kar
Conversion of stock in trade into capital asset

- Need for such change??
  - To make use of brought forward capital loss
  - To avail the concessional rate of tax applicable to long term capital asset

- Practice is not recognised expressly in the Act

- Permissible if the circumstances justify

- Risk of courts treating the above as a colourable device
Conversion of stock in trade into capital asset

- No tax upon such conversion in the absence of deeming provision - *CIT v. Sir Kika Bhai Premchand [1953] 24 ITR 506 [SC]*
Conversion of stock in trade into capital asset

• Upon sale, chargeable to tax as capital gains as nature of capital asset should be determined on the date of transfer and not on the date of acquisition as per Nachiappan [M] v. CIT [1998] 230 ITR 98 Mad.

• For computing capital gains – actual cost should be taken and not the converted costs as per

- Ranchhodbhai Bhaijibhai Patel (1971) 81 ITR 446 [Guj.]
- CIT vs. M. Ramaiah Reddy (1986) 158 ITR 611 (Kar)
- CIT vs. Vishwanath (1993) 201 ITR 920 (All)
- Keshavji Karsondas vs. CIT (1994) 207 ITR 737 (Bby)
Conversion of stock in trade into capital asset

- The period of holding in such case is to be reckoned from date of conversion as per Lohia Metals Pvt Ltd Vs ACIT 2009-TIOL-583-ITAT-MAD and Splendor Constructions (P) Ltd. vs ITO (2009) 122 TTJ (Del) 34

- Indexation

  - From the date of acquisition: Arun Sunny Vs DCIT184 Taxman-Mag 498 Cochin
  - From the date of conversion?
CONSIDERATION
Consideration

- Where consideration consists of only cash: Cash agreed to be given will be treated as full value consideration

- Where consideration consists of certain built up area

- Where consideration consists of partly cash and partly certain portion of built up area

- Where the agreement provides for
  - Refundable deposit
  - Non refundable deposit
Consideration – Built up area

- Nothing is taxable - Mahabodhi Society of India vs. UOI (1994), 209 ITR 412 (Cal) & Ashis Mukherji 222 ITR 168 Pat.

- Take the cost of construction: Applying the ratio of the order of the Delhi Bench of the Tribunal in the case of *M/s Vasavi Pratap Chand Vs. DCIT (89 ITD 73) (Del.*)* the consideration is the only the cost of construction of proposed building to the extent of which were falls to the assessee in the ultimately constructed area and not the market value of such share of constructed area which may be after the completion of the construction as per *DDIT Vs Shri G Raghuram 2010-TIOL-266-ITAT-HYD*

- Market value of that construction as on date of agreement is the amount to be taken into account for the purpose of determining the apparent consideration - *Ashok Leyland Finance Ltd v. Appr Authority (1998) 230 ITR 398 (Mad.*)*
Consideration – Built up area

- Market value was adopted in Shakuntala Rajeshwar’s case 160 ITR 840 Delhi

- Proper course of action may be to fix a certain consideration in agreement and providing that same will be discharged by way of allotment of certain specified built up area: CIT Vs Sri Ved Prakash Rakhra 210 Taxman 605 Kar

- Consideration in the form of flats – Applicability of section 54 and section 54F
Consideration – Section 50D

• Section 50D introduced by FA 2012 w.e.f 1.4.13

• Objective found in Memorandum

• Intending to undo Ms K Radhika Vs DCIT 2012-TIOL-90-ITAT-HYD

• Made prospective
Section 50D - Implications

- Reversal of principle in George Henderson 66 ITR 622 SC

- FMV of outgoing asset is taken as consideration

- When flats are received and finally sold

- When no flats are received but revenue is shared with the developer
Tax implication on sale of super built area

- Sale of super built area will have
  - Sale of built area
  - Sale of undivided interest in land

Separate treatment for the above two: The Statesman Ltd. vs. ACIT [2007] 112 TTJ (Kol) 593

Property booked with builder – Possession of property taken and sold thereafter immediately. Period of holding for long term capital gains to be reckoned from the date of booking of property and not the possession as per ACIT v. SHARAD THADANI 7 SOT 431 (Lucknow)
Incentives

- Section 54
- Section 54F
- Section 54EC
- Combination
- Section 80IB(10) if he participates in developing and building housing project
DEVELOPER
INCOME CHARACTERIZATION
Income characterization

a) In the hands of developers – Business income

b) In the hands of co-developers where there are more than one developer – Business income

c) Where the developer develops on own land:
   - Both land and building treated as stock
Income characterization – Use of own land held as capital asset

a) No automatic application of sec 45(2) as per CIT v. CHANDRIKA TOWERS [2005] 275 ITR 173 [MP]

b) Automatic application of sec 45(2)

- Tej Pratap Singh v. ACIT [2009] 177 Taxman (BN) i (Delhi)
Section 43CA

1. Section 43CA introduced by FA 2013 wef 1.4.2014

2. Memorandum – to provide treatment similar to section 50C even to stock in trade

3. See circular 3 of 2014
Section 43CA(2)/(3)/(4)

- The provisions of section 50C(2)/(3) shall, so far as may be, apply in relation to determination of the value adopted or assessed or assessable under 43CA(1).
- Where the date of agreement fixing the value of consideration for transfer of the asset and the date of registration of such transfer of asset are not the same, the value referred to in sec 43CA(1) may be taken as the value assessable by any authority of a State Government for the purpose of payment of stamp duty in respect of such transfer on the date of the agreement.
- The provisions of 43CA(3) shall apply only in a case where the amount of consideration or a part thereof has been received by any mode other than cash on or before the date of agreement for transfer of the asset.
Section 43CA(1)

1. Where the consideration received or accruing as a result of the transfer by an assessee of an asset (other than a capital asset),

2. being land or building or both, is less than the value adopted or assessed or assessable by any authority of a State Government for the purpose of payment of stamp duty in respect of such transfer,

3. the value so adopted or assessed or assessable shall, for the purposes of computing profits and gains from transfer of such asset, be deemed to be the full value of the consideration received or accruing as a result of such transfer.
METHOD OF ACCOUNTING
Income recognition

Different types of receipts by way of

- Sale consideration towards flat
- Vacant land tax,
- replacement fund,
- ground rent,
- maintenance charges,
- building insurance,
- transfer charges,
- fire fighting charges,
- security deposit,
- registration charges,
- electricity and water connection and electricity meter charges

See Aar Pee Apartments (P.) Ltd. v. ACIT [2010] 194 Taxman (Mag.) (Delhi-ITAT)
Income recognition

a) Completed contract method

- Upon completion of the contract
- Judiciary has taken note of this method
- Costs are captured and reflected as work in progress
- However, period costs like interest may be debited on a year to year basis. *Jt. CIT Vs. K. Raheja (P) Ltd.* (2007) 106 TTJ (Mumbai) 874
- In the year of completion, costs are debited and sales are credited to P&L Account

b) Proportionate completion method

- On the basis of proportion completed
Which method to follow?

a) AS 7
b) AS 9

c) TAS – Construction Contracts
d) Guidance Note on accounting of real estate transactions 2012
e) Guidance Note on recognition of revenue by real estate developers 2006
f) Ind AS 11 – Construction Contracts
g) Ind AS 18 – Revenue Recognition
h) TAS - Revenue Recognition
Case laws – Project Completion

• An assessee who is following project completion method & has constructed the residential complex on his own is out of the purview of revised AS-7 which is applicable in the case of construction contracts and recognizes %completion method and hence AO was not correct in ignoring project completion method and applying %completion method as per M/s Bhadrasen Construction 2010-TIOL-421-ITAT-MUM

• The correct procedure in ‘completed contract method’ is that instead of making addition, if some expenditure are found to be not allowable, the AO should correct the amount of WIP by reducing or enhancing WIP as the case may be as per Savala Associates [2009] 185 Taxman (BN–ii) Part 4
Case laws – Project Completion

• Other cases :

1. ACIT vs Kishandham Developers Pvt. Ltd (ITAT) Dated: 28th Feb 2011 - AS-7 vs Project Completion Method

Case laws – Proportionate Completion

• When prospective buyers of super build-up area giving consent to the terms of the two agreements namely, agreement to sell undivided interest in land and ‘agreement for construction’ which are enforceable legally by either party, assessee can naturally also transfer all significant risks and rewards to the buyers when these above agreements are authenticated by the parties involved in the said transaction.

• Such being the prevailing practice under JDA, assessee’s assertion that it will transfer ‘significant risk and rewards’ only after completion of project in spite of entering into said agreements is hypothetical.

• Prestige Estate Projects Ltd. v. DCIT [2011] 129 ITD 342 (Bang.)
Case laws – Proportionate Completion

- It is not right to say that unless and until the entire amount of expenditure to be incurred over the contract is known, no profit or gain can be calculated even if the contract moneys are received by an assessee in the course of the contract since as a rule the balance between cost of construction and proceeds of contract for the purpose of assessment under the Act has to be struck at an interval of every accounting year because that is the unit of time stipulated under the Act *Ramniklal J. Nathwani v. ITO [2009] 177 Taxman (BN) iv (Part-5)*

- Developer’s profit is referable to that part of the development of project which is completed; it is not necessary that all the flats should be first sold and then the project can be said to have been completed; each and every flat or unit is to be treated as an independent project and the profit on that part which has been completed by handing over the possession to the buyer cannot be postponed beyond the date on which the possession was handed over by the developer to the buyer as per *Growth Techno Projects Ltd. v. CIT [2009] 177 Taxman (BN) iv (Part-2)*
Case laws – Proportionate Completion

- The adoption of completed contract basis itself is a matter probably questionable in the case of developers. Even in the case of contractors, it is not strictly consistent with the Accounting Standards. The proper course is to make assessment on year to year basis. Such a view has been taken in

- **CIT vs. N. M. Associates** (2002) 256 ITR 141 (Mad),
- **Sri Sukhdeodas Jalan** (1954) 26 ITR 617 (Patna) and
- **M. A. Rauf vs. CIT** (1958) 33 ITR 843 (Patna).

- English law has also taken the same view in **Hughes vs. B. G. Utting and Co. Ltd.** (1940) 8 ITR (Suppl.) 57 (HL).
Incentives

- Section 80IB(10)
- Section 35AD
- Section 80IA(4)(iii) – Industrial Parks
- Section 80IAB – SEZ
- Business trusts
JOINT DEVELOPMENT

The Partners:

– Developer
– Co developer
– Land owner
In the case of a joint development agreement there is no adventure in the nature of trade as such a transaction is a barter.

CIT v. Smt. Radha Bhai (2005) 142 Taxman 595 (Del.)
JDA – A capital asset?

• JVA is a commercial deal providing respective rights and liabilities of parties relating to business agreed to be carried on but it was not a ‘business’.

• JVA is not merely a MOU not connected with the business as contended by the assessee.

• It is a commercial agreement but not ‘business’. The JVA could not be treated as ‘business’ as admittedly business agreed to be carried on was that of manufacture and sale of writing material and stationery.

• It was capital asset invested in the business but not business itself as per MS. PAYAL KAPUR V. ACIT [2006] 98 ITD 19 (DELHI)
JDA – Does it create an AOP?

• Faqir Chand Gulati vs Uppal Agencies Pvt. Ltd. & Anr (2014) TaxCorp(LJ) 2618 (SC) : Development agreements are NOT joint ventures

• Mere collaborative effort and the overall responsibility assumed by the applicant for the successful performance of the project is not sufficient to constitute an AOP : Hyosung Corporation, In re [2009] 314 ITR 343 (AAR)

• Where the association is not with the object of earning income but for co-ordination in executing the contract, no AOP is created :VAN OORD ACZ. BV, IN RE (2001) 248 ITR 399 (AAR)

• Indira Balkrishna [1960] 39 ITR 546 (SC) & Murugesan and Bros as held in the case of [1973] 88 ITR 432 (SC)
JDA – Does it create an AOP?

• Meeting of minds of members, common design and common purpose creates an AOP. Where a joint venture was created to provide project consultancy services and work was allotted to members, mere separate billing and members having separate bank accounts and each member to bear its own costs and expenses, do not derogate from existence of an AOP: GeocuonsIt ZT GmbH, In re [2008] 304 ITR 283 (AAR)
Section 50C & 55A
Section 50C

(1) Where the consideration received or accruing as a result of the transfer by an assessee of a capital asset, being land or building or both, is less than the value adopted (or assessed or assessable) by any authority of a State Government (hereafter in this section referred to as the "stamp valuation authority") for the purpose of payment of stamp duty in respect of such transfer, the value so adopted [or assessed or assessable] shall, for the purposes of section 48, be deemed to be the full value of the consideration received or accruing as a result of such transfer.

(2) Without prejudice to the provisions of sub-section (1), where –

(a) the assessee claims before any Assessing Officer that the value adopted [or assessed or assessable] by the stamp valuation authority under sub-section (1) exceeds the fair market value of the property as on the date of transfer;

(b) the value so adopted [or assessed or assessable] by the stamp valuation authority under sub-section (1) has not been disputed in any appeal or revision or no reference has been made before any other authority, court or the High Court, the Assessing Officer may refer the valuation of the capital asset to a Valuation Officer and where any such reference is made, the provisions of sub-sections (2), (3), (4), (5) and (6) of section 16A, clause (i) of sub-section (1) and sub-sections (6) and (7) of section 23A, sub-section (5) of section 24, section 34AA, section 35 and section 37 of the Wealth-tax Act, 1957 (27 of 1957), shall, with necessary modifications, apply in relation to such reference as they apply in relation to a reference made by the Assessing Officer under sub-section (1) of section 16A of that Act.
Section 50C

Explanation 1 - For the purposes of this section, "Valuation Officer" shall have the same meaning as in clause (r) of section 2 of the Wealth-tax Act, 1957 (27 of 1957).

Explanation 2.— For the purposes of this section, the expression "assessable" means the price which the stamp valuation authority would have, notwithstanding anything to the contrary contained in any other law for the time being in force, adopted or assessed, if it were referred to such authority for the purposes of the payment of stamp duty.

(3) Subject to the provisions contained in sub-section (2), where the value ascertained under sub-section (2) exceeds the value adopted [or assessed or assessable] by the stamp valuation authority referred to in sub-section (1), the value so adopted [or assessed or assessable] by such authority shall be taken as the full value of the consideration received or accruing as a result of the transfer.
Sec 50C - Snapshot

- Inserted by Finance Act 2002 w.e.f 1.4.2003

- Inserted with a view to tackle unaccounted income by practice of under-statement of consideration in acquisition of immovable property

- Similar attempt in the past made by section 52 - diluted by Apex Court decision - K.P.Varghese 131 ITR 597 (SC) & eventually omitted in 1988

- Alternate remedy for the Revenue was gift tax - omitted in 1998

- Chapter XXA was introduced (modified by Chapter XXC) empowering Central Government to acquire property which was sold below market value - eventually repealed

It is a rule of evidence placing responsibility on the seller to prove the apparent consideration to be real consideration.
Sec 50C - Snapshot

- Transfer of land or building or both
- **At a value less than the value adopted or assessed by Stamp Valuation authority (Stamp value)**
  - Capital gains = Stamp value - Cost of acquisition

  _If assessee disputes value adopted to exceed fair market value (FMV)_

  - AO may refer valuation to Valuation officer under section 55A
  - If FMV < Stamp value, Capital gains = FMV - Cost of acquisition
  - If FMV > Stamp value, Capital gains = Stamp value - Cost of acquisition

It is a rule of evidence placing responsibility on the seller to prove the apparent consideration to be real consideration.
Sec 50C - Some issues

• Is 50C constitutionally valid?

Section 50C cannot be said to be arbitrary because of adoption of guidelines value and violative of article 14 and principles of natural justice on the ground that no opportunity is given. Complete fullproof safeguard is to assessee to establish before the authorities concerned the real value - K.R. Palanisamy v. UOI [2008] 306 ITR 61 (Mad) & Bhatia Nagar Premises Co-operative Society Ltd. v. Union of India (2011) 334 ITR 0145 (Mum)

• Is section 50C applicable only to capital gains or business income as well?

As the property is treated as business asset and not as capital asset, there is no question of invoking the provisions of section 50C of the Act. Section 50C pertains to determining the full value of the capital asset.

– Inderlok Hotels P Ltd. v ITO 122 TTJ 145 (Trib. Mum.);
– CIT v Thiruvenqadam Investments P Ltd. 320 ITR 345 (Mad.);
– ACIT v Excellent Land Developers P Ltd. (2010) 1 ITR (Trib.) 563 (Del.)

• Is section 50C applicable to depreciable assets?

– ACIT v Roger Pereira Communications P Ltd. 34 SOT 64 (Mum)
– Panchiram Nahata v JCIT 127 TTJ 128 (Kol)
Sec 50C - Some issues

• Value to be adopted for section 54F investment - actual consideration or deemed value?

Gyan Chand Batra v ITO (2010) 133 TTJ 482 (Jaipur) & Gouli Mahadevappa v. ITO 135 TTJ (Bang.) 489

• Is section 50C applicable where sale deed is not registered?
  – Section 50C used the words “adopted or assessed”
  – Tribunal held 50C applicable only where sale deed is registered [Navneet Kumar Thakkar 110 ITD 525 (Jodh)(SMC)]
  – Finance (No. 2) Act, 2009 modified section 50C. Even if the value is “assessable”, section 50C would apply.
  – Explanation 2 inserted to define “assessable” to mean price which the stamp valuation authority would have, notwithstanding anything to the contrary contained in any other law for the time being in force, adopted or assessed, if it were referred to such authority for the purposes of the payment of stamp duty

• Does adjustment under section 50C attract penalty under section 271(1)(c)?

  No penalty to be levied since there is no concealment
  – ACIT v N. Meenakshi (2009) 125 TTJ 856 (Chennai)
  – Prakash Chand Nahar 110 TTJ 886 (Jodh.)
Sec 50C - Some issues

• Is section 50C mandatory?
  – Once the assessee applies to AO for making reference for valuation, “may” becomes “shall”. Therefore, if assessee applies, AO shall make reference to DVO. It is not optional for AO to make reference to DVO. It was held that right of assessee u/s. 50C is a valuable statutory right available to protect his interest against arbitrariness which may creep in while fixing the value of capital gain and it is the safeguard given to the assessee - N. Meenakshi 226 CTR 625 (Mad)
  – The said right is more effective in cases where the parties to the document have not taken any steps to defend or to initiate proceedings under Stamp law - Jitendra Mohan Saxena 117 TTJ 974 (Trib Luck.)

• Can there be instances where section 50C is not invoked?
  – Distress sale
  – Exigency of funds
  – Haunted premise
Section 55A

With a view to ascertaining the fair market value of a capital asset for the purposes of this Chapter, the Assessing Officer may refer the valuation of capital asset to a Valuation Officer -

(a) in a case where the value of the asset as claimed by the assessee is in accordance with the estimate made by a registered valuer, if the Assessing Officer is of opinion that the value so claimed is less than its fair market value;

(b) in any other case, if the Assessing Officer is of opinion -

(i) that the fair market value of the asset exceeds the value of the asset as claimed by the assessee by more than such percentage of the value of the asset as so claimed or by more than such amount as may be prescribed in this behalf; or

(ii) that having regard to the nature of the asset and other relevant circumstances, it is necessary so to do, and where any such reference is made, the provisions of sub-sections (2), (3), (4), (5) and (6) of section 16A, clauses (ha) and (i) of sub-section (1) and sub-sections (3A) and (4) of section 23, sub-section (5) of section 24, section 34AA, section 35 and section 37 of the Wealth-tax Act, 1957 (27 of 1957), shall with the necessary modifications, apply in relation to such reference as they apply in relation to a reference made by the Assessing Officer under sub-section (1) of section 16A of that Act.

Explanation.—In this section, "Valuation Officer" has the same meaning, as in clause (r) of section 2 of the Wealth-tax Act, 1957 (27 of 1957).]
Sec 55A - Snapshot

- Specific powers to AO for referring to Valuation Officer if in the opinion of AO the value of the asset as claimed by the assessee is less than the FMV of the asset

- Scope confined to ascertainment of FMV

- Placed in Part E of Chapter IV (Capital gains) - confined to capital gains

- Minimum value of Rs 25,000 & undervaluation by at least 15% (Rule 111AA)

- Section 142A inserted by Finance Act 2004 to enlarge the powers under section 55A z; Fall out of Amiya Bala Paul (2003) 262 ITR 407 (SC)
Sec 55A - Issues

► Is valuation expected to give true and correct market value?
  – Dilip N Shroff v JCIT (2007) 291 ITR 519 - market value to be different based on locale of the property

► Whether making a reference prevents ITO from estimating value on his own?
  – *No procedural provision of the Act should be interpreted in a manner to defeat the goal which the procedure seeks to achieve. The entire procedure is to facilitate the determination of the value of various assets to expedite the completion of the assessment. The said provision cannot be interpreted in a negative manner so that the provision becomes counterproductive and a clog in the proceeding. It cannot be said that once having referred the case of valuation to the DVO, the Assessing Officer is totally robbed of his jurisdiction.*

{Shahdara (Delhi) Saharanpur Light Railway Co. Ltd. v CIT (1994) 208 ITR 882 (Cal)}
Sec 55A - Issues

► Can there be reference to valuation without rejecting books?

*Sargam Cinema v. CIT [2010] 328 ITR 513 (SC)* If Books of account of assessee are not rejected, Assessing Officer cannot refer matter to Departmental Valuation Officer.

► Can valuation report be the basis for reassessment?

- *No as per ACIT v. Dhariya Construction Co. [2010] 328 ITR 515 (SC)*
Sec 55A - Issues

- Whether formation of opinion of the Assessing Officer that the value claimed by the assessee less than its fair market value is sine qua non?
  - CIT v Umedbhai International (P) Ltd.

- Can reference be made after completion of assessment?
  - It is abundantly clear that for computation of income falling under Chapter IV of the Income-tax Act, the ITO may refer the matter of valuation of a property to the Valuation Officer only when the assessments are still pending. There is no authority under the said provisions of section 55A to refer case for valuation of a property after the assessment is completed by the ITO - Bhola Nath Majumdar v. ITO (1996) 221 ITR 608 (Gau)