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ORGANISED By: ***WIRC of ICAI***
SUBJECT: Redevelopment Tax Implications on (Tenant, Ownership, CHS,Taxation of Joint Venture)
DATE & DAY: 18th November, 2017 (Saturday)
Time: 06.00 PM TO 08.00 PM
VENUE : ICAI Tower, Plot No.C-40, 'G' Block, Bandra Kurla Complex, Bandra (E), Mumbai – 400 051

BY CA VIMAL PUNMIYA

1. INTRODUCTION

Income – tax Act, 1961 (hereinafter referred to as 'The Act') is the legislation of our country which refers various central acts and various state legislations. To understand the various taxation issues relating to Real Estate Transactions, it is very essential to know the provisions of general law with special reference to Transfer of Property Act, Registration Act, Stamp Act, Development Control Regulations, etc. In this paper we have made an attempt to discuss some of the very important taxation issues relating to Real Estate Transactions.

2. METHODS OF ACCOUNTING:-

Taxation of the real estate transaction largely depends upon accounting method followed by the entities. Till date specific method was not recognized by the legislature. Therefore, entities are free to adopt any method which they feel appropriate for them. Most of entities follow either a) Project completion method or b) Percentage completion method. In case of ***CIT v/s Bilahari Investments (P) Ltd. [(2008) 299 ITR 1 SC]*** *it was held that Recognition/identification of income under the Act, is attainable by several methods of accounting. It may be noted that the same result could be attained by any one of the accounting methods. Completed contract is one such method. Similarly, percentage of completion is another such method.*

a. PROJECT COMPLETION METHOD

A method of recognizing revenues and costs from a long-term project in which profit is recorded only when the project has been completed. Even if payments are received while the project is in progress, no revenues are recorded until its completion. The Project completion method (Also known as completed-contract method) is a conservative way of accounting for long-term undertakings and is used for certain types of construction projects.

b. PERCENTAGE COMPLETION METHOD

Method of recognizing revenues and costs from a long-term project in relation to the percentage completed during the course of the project. Thus, the percentage of completion method allows a business profits (or losses) on a project before its completion.

c. PROBLEM FACED BY ASSESSEE IN ASSESSMENT PROVISIONS RELATED TO METHOD OF ACCOUNTING

The common issued raised by the department is related to method of accounting. Department wants to tax income on percentage completion method, so tax can be collected at every year on basis of % of completion. But assessee wants to offer income for tax on completion of project. So, funds can be used for business purpose and tax will be paid when project actually gets over in all aspects. Hence, no uncertainty remains with costing part and actual income offered for tax. Because in percentage completion method, if later costs get increased it was difficult to justify profit ratios from earlier years. Situation get difficult if when assessee offered income in earlier years and later on due to increased in cost he suffered from loss. In that situation their funds also got blocked in tax and they need to carry forward the loss to next 8 years.
The common grounds taken by department for following percentage completion method and stand taken by assessee are as follows:-

SN	Department Ground	Assessee Stand
1	*Project Completion method is not applicable as on date*	*Project Completion method is a recognized method of accounting and cannot be disturbed.* ***CIT V/s Umang Hiralal Thakkar 2014] 42 taxmann.com 194 (Gujarat HC)***
2	*Accounting Standards are compulsory in nature.*	*Accounting standard issued by the ICAI is recommendatory in nature cannot enforced on Assessee, because only AS-1 & AS-2 were recognized under Income tax.* ***Aditya Builders V/s CIT [2013] 39 taxmann.com 178 (Mumbai - Trib.) with strong wording held that:-*** *Whether revenue cannot thrust a method of accounting on assessee though that method is superior - Held, yes* *Whether, therefore, where assessee had been consistently following project completion method in respect of his two projects, Commissioner was not justified in directing AO to compute income of assessee from one project by applying percentage completion method - Held, yes* ***Paras Build tech India Pvt. Ltd. Vs CIT ITA 602/2015 (Del HC)****:-* *The settled legal position as far as Section 145 is concerned is that it is not open to an AO to reject the accounts of an Assesses unless he comes to a determination that notified accounting standards have not been regularly followed by the Assesses. As pointed out by the CIT (A) in the order dated 2nd July, 2010, <u>the AS of the ICAI did not have any statutory recognition under the Act</u> although it was binding under the Companies Act, 1956. The method of accounting followed by the Assesses in the present case i.e. project completion method was certainly one of the recognized methods and has been consistently followed by it.*
3	*As per AS-7 Only percentage completion method is applicable*	*AS 7 (issued in December 1983), originally recognised two methods of computation namely the completed contract method and percentage of completion method. Besides, the Standard was applicable not only for construction contracts but also to enterprises undertaking construction activities on their own account as a venture of commercial nature where the enterprise has entered into agreement for sale.* *Accounting Standard 7 was revised in 2002 to recognise only percentage of completion method for accounting of income. Thus, completed contract method has been de-recognised. Besides, it applies only to construction executed in pursuance of contracts and*

		not to projects executed suo motu. *The implication is that in respect of own projects of the building AS-7 does not apply.* ***Sabh Infrastructure Limited, New Delhi vs. DCIT, Circle 7(1), vide ITA No. 4572(Del) of 2009***
4	*When project in initial stage department take plea that in earlier year only small work was done, therefore, it cannot be held that project completion method was followed or not?*	*For determination of method of accounting regularly employed for initial year will be taken from sub-sequent years. Assessee followed in sub-sequent year project completion method. Then it will be treated that assessee has followed project completion method in earlier year also.* ***CIT v. Smt. V. Sikka [1984] 149 ITR 73 Delhi High Court****:-* *Even for the first year, the method of accounting is deemed to have been employed if the same is shown to have been regularly employed in subsequent years as is also the case in appeal. The real estate developer is not a pure contractor but is a seller of flats/goods. It is not mandatory for all real estate developers to follow percentage completion method as prescribed by Institute of Chartered Accountants of India under AS-7.*

d. EFFECT OF INCOME TAX COMPUTATION DISCLOSURE STANDARDS (ICDS) ON PROJECT COMPLETION METHOD ANDCASES PENDING BEFORE APPELLATE AUTHORTIES:-

Section 145(2) empowers CBDT to issue Income Tax Computation Disclosure Standards (ICDS) for computation of total income. ICDS III relates to construction contract and recognize only percentage completion method. However, ICDS III revenue recognition does not provide the clear contention that whether it will apply on real estate developer or not who developer project on their own risk. And due to complexity of these ICDS and Business oprendi of Real Estate Developer, this is not practical to follow that ICDS. Therefore, Direct Taxes Committee of ICAI made detailed representation to Central Board of Direct Taxes during the Direct Tax Workshop with CBDT which was followed by written representation to Chairman, CBDT on 31.03.2016 and Hon'ble Finance Minister, on 7.04.2016. On invitation by CBDT subsequently, the ICAI representatives met Joint Secretary (TPL-I) and Director (TPL-III) at North Block, New Delhi on 18th April, 2016 and 27th April, 2016 and made detailed presentation on difficulties that would be faced by stakeholders on implementation of ICDS. The representations made by ICAI were considered positively by the Expert Committee on ICDS in meeting held on 12.05.2016 and ICAI was asked to prepare detailed FAQs and amendments to ICDS which were submitted on 20.05.2016. The FAQ No. 15 deal with above point which is as under:-

Question 15: Since there is no specific scope exclusion for Real estate development activity and BOT projects from ICDS IV on Revenue Recognition, please clarify whether ICDS III and IV should be applied by real estate developers and BOT operators. Also, there is no specific exclusion for lease income in ICDS IV. Please clarify whether ICDS IV is applicable for lease income.

Answer: The Accounting Standards Committee has recommended that separate ICDS should be notified for real estate development activity, BOT projects and Leases. A draft ICDS on Leases was also published for public comments but not finally notified. Hence, pending notification of specific ICDS to deal with these revenue items, they shall continue to be governed by existing tax laws. It is clarified that ICDS III and ICDS IV do not apply to these business activities.

Thus, As per ICAI it is clarified that revenue recognition of real estate developer will not be governed ICDS III.

Later on CBDT come up with Draft ICDS REAL ESTATE TRANSACTIONS vide press release dated 11/05/2017. In this ICDS also only percentage completion method proposed and in PARA 7 transitional provisions also proposed. As per transitional provisional cut out date will be provided when ICDS will issue for following percentage completion method. Project started before cutoff date will be taxed as per the method followed by the assessee. So till cutoff date not decided, project completion method is recognizing method of accounting which CBDT also accepted. So assessee can take shelter of this ground in all pending appeals or assessment proceedings.

e. CHANGE OF METHOD OF ACCOUNTING

Disclosure of changes in an accounting policy used for construction contracts should be made in the financial statements giving the effect of the change and its amount. However if a contractor changes from the percentage of completion method to the completed contract method for contracts in progress at the beginning of the year it may not be possible to quantify the effect of the change. In such cases disclosure should be made of the amount of attributable profits reported in prior years in respect of contracts in progress at the beginning of the accounting period.

It is held that the assessee having changed his method of accounting from work-in- progress in original return to project completion method in revised return, assessment had to be made as per revised return.

Satish H. Patel [93 TTJ 458 (Pune)]

f. DISCLOSURE IN THE COURSE OF SEARCH – WHETHER INCOME MUST BE TAXED ON COMPLETION OF THE PROJECT?

The conduct of search and seizure operation in a particular year does not lead to an inference that the undisclosed income detected as a consequence thereof has to be taxed in the assessment year relevant to the previous year in which search was conducted. In other words, accounting of profits has yet to be made on the basis of method of accounting followed by the assessee.

It is held that Undisclosed income in the form of 'on money' stood established by seizure of document r/w statement recorded under s. 132(4); however in computing undisclosed

income, expenditure incurred has to be allowed; income discovered has to be taxed in assessment years as per method of accounting followed by assessee.

Dhanvarsha Builders & Developers (P) Ltd. vs. DCIT [(2006) 102 ITD 375 (Pune)]

Methodology ought to be adopted to assess income embedded in such undisclosed receipts, as has been accepted by the Revenue in the regular assessments

Arth Housing Development Pvt Ltd. v/s ACIT Central Circle-25 ITA No.6764/Mum/2010

3. <u>FINANCE COST, INDIRECT COST AND COMPUNDING CHARGES.</u>

A. INTEREST ON BORROWED CAPITAL –

As per clause 2(1)(b)(iii) of ICDS IX all inventory which require 12 months or more to bring them to a saleable condition are qualifying assets and borrowing cost incurred for that inventory will be capitalized into cost of that asset and will be allowed when income from that project offered for tax. As the real estate project takes more than 12 months to bring them saleable. So, borrowing cost incurred on that project will be part of cost of project and allowable in the year when project offered for tax.

Clause (2)(1)(c)(A.)(ii) of Draft ICDS on real estate transaction also considered borrowing cost as cost of project and will be allowed against project revenue when revenue will be offered for tax.

B. ADVERTISEMENT EXPENSES TO BE CAPITALISED AS WORK-IN-PROGRESS

It is held that Assessee following project completion method, and advertisement expenses of the two projects being allocable to individual project, such advertisement expenses have to be capitalized as work – in – progress to be allowed deduction in the year of completion of project.

ITO V/s Panchvati Developers [115 TTJ 139 (Mum)]

C. WHETHER COMPOUNDING CHARGES PAID BY BUILDERS ALLOWED AS A DEDUCTION

In this case it was held in the order passed by a competent authority of Town Planning in unmistakable terms stated that he had permitted the payment of compounding charges by erring builders to regularize the infirmity in the building construction. There could not be any doubt that what had been done was to permit the assessee to compound the offence committed by it putting up an unauthorized construction.

Explanation to Sec. 37(1) defines that any expenditure incurred for any purpose which is an offence or which is prohibited by law is not entitled to deduction. Hence compounding of the offence under Corporation Act cannot take away the rigour of explanation to sec 37 and the deduction is not available.

Mamta Enterprises – [135 Taxman 393 (Karnataka.)]

4. <u>TAXATION OF UNSOLD FLAT:-</u>

By inserting sub-section (5) to section 23 legislature put bar on all the controversies on taxation of unsold flat held as stock in trade. Now, annual value (as per section 23) of all unsold flats held as stock in trade retain by developer for more than 1 year from end of the financial year in which completion certificate granted by the competent authority will be taxable under house property head .

5. PROPERTY V/S BUSINESS INCOME

Earlier rental income earned by real estate developer was not of dispute, because developers preferred to offer income under house property head so then can claim standard deduction of 30%. But department wants to tax rent income under business head.

This issue was resolved by Hon'ble Supreme Court in **Shambhu Investment (P) Ltd. v. CIT (2003) 263 ITR 143 (SC)** where is was held that "*income derived from letting assessable as income from property and not business income.*

Legislature also by inserting sub-section (5) to section 23 clarified that unsold flat are taxable under house property head. Hence, unsold flat is taxable under house property head, than, flat given on rent by real estate developer will also be taxable under house property head.

Renting income will be taxable under business head only in one condition, i.e. when renting property is main business activity of assessee.

M/s Chennai Properties & Investment Ltd. V/s CIT Central III CA No.4494 of 2004

6. INTEREST EARNED ON SURPLUS MONEY PARKED AS FIXED DEPOSIT WITH BANK TAXED UNDER THE HEAD THE BUSINESS.

It is held that advances from customers intending to purchase flats, deposit of surplus money with bank in course of business – the accrued interest arises out of business activities hence such interest income assessable as business income and not as income from other source.

CIT V. LOK HOLDINGS 308 ITR 356 (BOM.)

7. CAPITAL GAIN vs. BUSINESS INCOME and CONVERSION

Whether a particular asset is stock-in-trade or capital asset does not depend upon the nature of the article, but the manner in which it is held. The same item may be stock-in-trade in the hands of the assessee who deals in that item. But it will be capital asset in the case of an assessee who uses it for earning income or holds as an investment. For example, a dealer in real estate holds a piece of land or house property as stock-in-trade. But it will be a capital asset in the hands of a person who holds it as an investment and derives income from leasing or renting of the property.

Even stock-in-trade may become capital asset in certain circumstances and *vice versa*. If an assessee who deals in certain goods or commodities as trader, on closure of the business, retains the existing stocks as investment, the stocks will become capital asset in his hands from the time of closure, not withstanding that they were stock-in-trade earlier in his hands. Even in the course of a business, an assessee may try to transfer some of the stock-in-trade from his trading activity and decide to hold them as investment.

The stocks so held would assume the character of capital asset from the date of such holding. This may usually happen in the case of dealer in shares and real estate. But in all these cases, the finding will be one of fact depending upon the intention and conduct of the assessee supported by direct and circumstantial evidence.

In CIT vs. Bright Star Investments (P) Ltd. (2008) 24 SOT 288 (Bom.) it was held that IT Act does not contain a provision similar to section 45(2) with respect to conversion of stock-in-trade to capital asset. It was further held that holding period is to considered from the date of acquisition.

However, in Splendor Constructions (P) Ltd. vs. ITO (2009) 27 SOT 39 (Delhi)/ 122 TTJ 34 it was held that the period to be considered from the date of conversion to investment. This decision has not considered the above decision of the Mumbai Tribunal in Bright Star.

Similarly, when a capital asset is converted into stock-in-trade, the same will no longer be capital asset. However, this situation is covered by section 45(2).

As per section 45(2) if a capital asset is converted into stock-in-trade, the capital gain is taxable in the year such stock is sold, and the fair market value of the asset on the date of such conversion or treatment shall be deemed to be the full value of consideration received or accruing as a result of the transfer. Thus capital gain gets computed by taxability is postponed to the year of sale of such converted capital asset i.e., stock-in -trade.

8. DEVELOPMENT RIGHTS:

DEVELOPMENT RIGHTS – WHO ARE ENTITLE – SOCIETIES OR MEMBERS?

In respect of Tenants co-partnership co-operative societies, which are of the nature of “Flat Owners Societies” in which the flats are acquired by the society from the builder on ownership basis and thereafter Society is formed, and land is conveyed to the society and individual members acquire ownership rights over the building and underneath the development rights.

This concept has been recognized under Bombay stamp Act as on the conveyance in favour of the housing societies, stamp duty paid by the purchasers of flats on ownership agreements is deducted from the stamp duty payable on the market value of the property transferred in favour of the society as per proviso to article 25 of schedule 1 of Bombay Stamp Act.

Circular No. F.N. 4 / 28 / 68 – WT DT. 10.0.1969 AND 27.01.1969 explaining the provisions of section 5(1)(iv), the Board clarify that flats vest with individual members of society and wealth tax exemption will be available to individual members.

[I] AREA

Liability of Income/Capital Gain Tax, if any, on:-

(A) Additional area in the hands of individual members.

Ans. As per Section 54 of the Income Tax Act, 1961, if any residential property which was held for a period of more than 2 years is sold or given for redevelopment and the new flat is

purchased or acquired within a period of 1 year before or 2 years after the sale or constructed within 3 years after the sale then capital gain arising on the transfer of the old flat will be exempt to tax u/s. 54 of the Income Tax Act, 1961 to the extent of the cost of such new flat.

In the case of redevelopment, the new flat to be acquired is treated as constructed for the purpose of the Section 54. Thus, if the new flat is acquired by the owner within a period of 3 years from the surrender of the original flat then the capital gain arising from the sale of the original flat can be claimed to be exempted u/s. 54 of the Income Tax Act.

If the new flat is not acquired by the owner within a period of 3 years then the Assessing Officer at his discretion can disallow the same at any time during the assessment.

However, allotment of a flat or a house by a cooperative society, of which the assessee is the member, is also treated as construction of the house [Circular No. 672, dated 16-12-1993]. Further, in these cases, the assessee shall be entitled to claim exemption in respect of capital gains even though the construction is not completed within the statutory time limit. [*Sashi Varma* v *CIT* (1997) 224 ITR 106 (MP)]. Delhi High Court has applied the same analogy where the assessee made substantial payment within the prescribed time and thus acquired substantial domain over the property, although the builder failed to hand over the possession within the stipulated period. **[*CIT* v *R.C. Sood* (2000) 108 Taxman 227 (Del)].**

Hence, relying upon the above judgments, even if in the case of development, the new flat is acquired by the owner after a period of 3years from the surrender of the old flat, an assessee can claim exemption u/s. 54.

If the new flat acquired to claim exemption u/s. 54 is sold within a period of three years from the date of purchase then the capital gain exemption claimed earlier would become taxable in the year the new flat is transferred.

Thus, Receipt of extra carpet area over and above the existing area could be claimed as exemption u/s. 54 of the Income Tax Act,1961.

Further, we would like to state that under the definition of “Transfer” according to Sec 2(47) Income Tax Act, 1961, transfer, in relation to a capital asset, includes sale, exchange, or relinquishment of the asset or the extinguishment of any rights therein or the compulsory acquisition thereof under any law.

An exchange involves the transfer of property by one person to another and reciprocally the transfer of property by that other to the first person. There must be a mutual transfer of ownership of one thing for the ownership of another. Hence, the acquisition of new flat would be considered as exchange and would be considered as transfer for the purpose of capital gain.

Argument could not be made that no cost is incurred by any member for the acquisition of the new flat and hence capital gain cannot be computed and the case does not fall within

the ambit of Section 55(2). The member is forgoing his rights in the old flat. And hence, it would be considered as the cost of acquisition of the new flat.

However, if the residential flat is held for a period of less than 3 yrs than the receipt of extra area by the individual members would be taxable in the hands of the individual members.

(B) Cash compensation received upon surrender of entitled additional area, in part or in full, by an individual member.

Ans. If the Individual member is surrendering a part of the existing area then the Individual member would be liable to pay Capital Gain Tax. The sale consideration would be calculated as per **Section 50C of the Income Tax Act**, which is as follows:

“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 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.”

However, if the Individual member is surrendering a part of the additional area then the Individual member would not be liable to pay any income tax or capital gain tax on the same.

(C) The Society for receiving amenities and facilities for the common use of its members and their families.

Ans. If the Society is receiving for amenities and facilities for the common use of its members and their families then the same is not taxable in the hands of the Society or the Individual members as there is no cost of acquisition of the same.

In deciding the case of ***JETHALAL D.MEHTA V. DY. CIT [(2005) 2 SOT 422 (MUM.),*** Hon. Income Tax Appellate Tribunal mainly relied upon Supreme Court decision in the case of ***CIT V. B.C.SRINVASA SHETTY 128 ITR 294*** in which it was decided that if there is no cost no capital gain can be worked out hence amount received is to be treated as exempt receipt.

II] Corpus Money expected at Redevelopment

Liability of Income/Capital Gain Tax, if any, on:-

(A) Corpus Money received by the individual members from the Developer in lieu of surrender of part entitlement of FSI/Development rights.

Ans. If the Individual member is receiving an area which is same or more than the present area then the Individual member is not liable to pay capital gain tax on the same.

If however, Individual member is receiving an area which is less than the present area than the Individual member is liable to pay Capital Gain Tax as per Section 50C of the Income Tax Act, 1961 as already explained above.

(B) Corpus Money received by the Society from the Developer in lieu of surrender of part entitlement of FSI/Development Rights, such funds being invested by the Society to earn interest income to meet/subsidize the maintenance costs of its Redeveloped premises and property.

Ans. If at the time of Redevelopment, the Society was in not in possession of unutilized FSI/Development Rights, then the Society would not be liable to pay any Capital Gain Tax on the receipt of the Corpus Money on surrender of a part of FSI/Development Rights.

Further, if the Society has unutilized FSI/Development Rights in its possession at the time of Redevelopment, then the receipt of the Corpus Money on surrender of the part of FSI/Development Rights would be taxable in the hands of the Society.

Also, in the case of (1) ***New Shailaja CHS v. ITO (ITA NO. 512/M/2007. BENCH B dated 2nd Dec, 2008 (mum.)and (2) ITO v. LOTIA COURT CO- OP. HSG. SOC. LTD. (2008) 12 DTR (MUMBAI)(TRIB) 396*** it was held that *where the assessee, a Co-op. Hsg. Soc. Ltd. Became entitled, by the virtue of Development Control Regulations, to Transferable development Rights (TDR) and the same was sold by it for a price to a builder , the question arose whether the transaction of sale receipt could be taxed. It was held that though the TDR was a Capital Asset, there being no 'cost of acquisition' for the same, the consideration could not be taxed.* The same is held in the cases of **NEW SHAILAJA CHS LIMITED (ITA NO. 512/MUM./2007), OM SHANTI CO-OP. HSG. SOC. LTD. (ITA NO.2550/MUM./2008)** & **LOTIA COURT CO-OP. HSG. SOC. LTD. (ITA NO. 5096/MUM./2008).**

Further, in the case of **MAHESHWAR PRAKASH 2 CHS LTD. 24 SOT 366 (MUM.)**, it was held that *the assessee-society acquired the right to construct the additional floors by virtue of DCR, 1991 which could not be available to the assessee on expenditure of money. Prior to DCR, 1991, no society had any right to construct the additional floors, so it was not a tradable commodity. Suddenly by virtue of DCR, 1991, the right was conferred by the Government on the assessee. Such right exclusively belonged to the building owned by the society. It could not be transferred to any other building.*

Similarly, similar right belonging to other societies could not be purchased by the assessee for the purpose of constructing additional floors in its own building. Therefore, such right had no inherent quality of being available on expenditure of money and, therefore, cost of such asset could not be envisaged. Hence, the said view was fully justified in terms of the decision of the Apex Court in the case of B.C. Shrinivasa Shetty.

Therefore, the right acquired by the assessee did not fall within the ambit of section 45 itself. The amended provisions of section 55(2) were also not applicable, since such right was not covered by any of the assets specified in section 55(2)(a).

Therefore, the sum of Rs. 42 lakhs received by the assessee from the developer was not chargeable to tax under section 45. Therefore, the impugned orders passed by the lower authorities were to be set aside.

(C) Corpus Money received by the Society from the Developer (as described in B above) and subsequently distributed to its members.

Whether such incomes enlisted above at A, B and C, if taxable, shall be treated as Capital Gains or deemed to be income earned in the year of receipt.

Ans. As per Maharashtra Co-op. Societies Act, 1960, a Co-operative Society cannot distribute the corpus funds to its Individual member, it can only declare dividends. However, the declaring of Dividends has lots of restrictions and formalities.

(D) Liability of Income Tax, if any, on interest income arising from investment of such Corpus Money by the Society/individual members in the Co-operative/other Banks.

Ans. If the Society receives interest income form a Co-operative bank then the same is exempt from tax. And, if the interest income is received from other banks than the same is taxable and the Society has to pay tax on the same.

However, as per Hon'ble **Tribunal Judgment** in the case of **ITO v. Sagar Sanjog C.H.S. Ltd., ITA Nos. 1972 to 1974 and 2231 to 2233/ Mum./ 2005(BCAJ)** it was held that *the interest income earned out of the fund money invested went to reduce the maintenance. According to the tribunal, the interest would have been taxable, had there been surplus left after it being adjusted against the maintenance expenses. The tribunal also noted that there was nothing on record to suggest that the interest income would be given to members on dissolution of the Society.*

Thus, even the interest income received from other than Co-operative Bank and spent on Society's work then the concept of Mutuality will apply and is not liable to tax but this view is not free from litigation.

III] Rent for Temporary Alternative Accommodation including Deposits, if any:

Rental allowance may be received by individual members in the event of need for Relocation during Redevelopment. Such amounts may be utilized in part or in full towards rent paid for alternative premises or may remain entirely unspent if the member already has his/her own alternative accommodation. Such allowance may be received for about three years, either together in one tranche in advance or in installments on a staggered basis.

Liability of Income Tax, if any, on such Rental Allowance, including Deposits, if any, received by the individual members.

Whether such income, if taxable, shall be treated as income earned in the year of receipt (if received on a staggered basis) or entirely as income in one year (if received fully in advance)

Ans. In order to get the old building redeveloped, the existing structure of the old building is required to be demolished and hence, it is necessary to vacant the same. To facilitate redevelopment and to compensate the flat owners for the hardship to be faced by them in this regard, the Developer might offer them Rent compensation which they would be paying for the temporary accommodation during the period of redevelopment.

The Rent Compensation so provided by the developer to the owner should be expended by the owners for the purpose of their temporary accommodation and other expenditure related thereto.

If the actual rent paid by the flat owners is less than the Rent compensation received by them from the redeveloper then the excess of such amount received will be taxable under the head **Income from Other Sources,** otherwise, the Rent compensation received by the flat owners from the redeveloper is not taxable.

The Rent Compensation given to the Individual Members shall be taxable in the year of receipt if the Rent Compensation is received on staggered basis and the whole is not spend by the Individual Members on their alternative accommodation.

However, if the Rent Compensation is given to the Individual Members in one tranche in advance, then the Rent Compensation received by the Individual Members would be taxable on proportionate basis if the same is not spend on the Alternative Accommodation.

IV] Hardship Allowance/ Compensation for Inconvenience.

Members opting not to be temporarily relocated during the Redevelopment may receive "Hardship Allowance" from the Developer.

Members agreeing to be temporarily relocated during Redevelopment may receive "Compensation for Inconvenience" from the Developer.

Liability of Income Tax, if any, on such Allowance/ Compensation and if taxable, mode of computation i.e. whether as income in the year of receipt or whether on a staggered basis as received.

Ans. Along with extra area and Rent compensation, the redevelopers also offer lumpsum amount to the flat owners in addition to extra area and compensation. The transfer of TDR to Builder for development of property does not attract Capital Gain Tax.

In deciding the case of ***JETHALAL D.MEHTA V. DY. CIT [(2005) 2 SOT 422 (MUM.),*** Hon. Income Tax Appellate Tribunal mainly relied upon Supreme Court decision in the case of ***CIT V. B.C.SRINVASA SHETTY 128 ITR 294*** in which it was decided that if there is no cost no capital gain can be worked out hence amount received is to be treated as exempt receipt. Hence, the Hardship Allowance and the Compensation for Inconvenience is not taxable in the Hands of the Individual Members as Hardship Allowance and Compensation for Inconvenience can't be worked out in monetary terms and have no cost. Since there is no cost of acquisition, as per Income Tax Act, 1961, the receipt would not be treated as a Capital Receipt and thus, is exempt from tax.

V] White Goods/ Household Amenities received by Members from Developer.

Liability of Income Tax, if any, on individual members for White Goods/Household Amenities such as Air-Conditioners, washing machine, modular kitchen, etc. that are sometimes included by Developers in the new premises on a complimentary basis.

Ans. All the White Goods/ Household Amenities which are attached to the Flat i.e. Fixtures, Modular Kitchen, Centralized A/c, etc. are treated as a part of the Flat and thus, are exempt and not taxable in the hands of the Individual Members.

Other Movable items such as Refrigerator, Sofa Set and other furniture which are not attached to the walls of the flat and exceeds 50,000/- in value in totality are not treated as a part of the Flat and are thus taxable in the hands of the Individual Members in the year of receipt of such amenities u/s. **56(2)(x) of the Income Tax Act, 1961**.

VI] Reimbursement of Expenses from Developer.

Liability of Income Tax, if any, on the Society/ individual members for Reimbursement from Developer of Expenses such as Stamp Duty, Fees of Consultants (Architect, Lawyers, Chartered Accountants, etc.) cost of updating members and holding General Body meetings, Administrative Expenses towards the Redevelopment Process, etc. incurred/ to be incurred.

Ans. Anything amount which is reimbursed by the Developer is not taxable either in the hands of the Society or the Individual Members, provided that the entire amount of reimbursement is been spent on the expenses it is reimbursed for.
Thus, if excess amount is reimbursed by the Developer than the amount which is actually spent for the purpose than the excess amount would be taxable on the receipt of the same.

However, in the case of a Society, if excess amount is reimbursed to a Society by the Developer than actually spent by the Society, and the excess amount so received is been used by the Society for payment of expenses which are for the welfare of the Society or the Individual Members than the excess amount received by the Society would not be taxed and hence, would be exempt. Otherwise the excess amount received by the Society would be taxable.

VII] Liquidation & Disbursement of Existing Sinking Fund.

Liability of Income/Capital Gain Tax, if any, on the Society/ individual members upon liquidation and disbursement to existing members (with permission from Registrar/any other authority) of existing, unutilized Sinking Fund (generated by annual contributions from members and bank interest earned thereon.) prior to induction of new members arising from saleable portion of Redeveloped premises.

Ans. In our view, the Sinking Fund is to be used on the property itself either for the purpose of development or Heavy Repair. However, if the Registrar gives permission then the Sinking Fund could be distributed amongst the Individual Members which again has a number of restrictions.
This distribution of Sinking Fund after the permission of the Registrar would be taxable in the hands of the Individual Members to the extent of the interest on such a fund. The distribution of the principal amount would not be taxable in the hands of the Society or the Individual Members.

VIII] TDS on receipt.

Whether tax shall be deducted at Source (TDS) from Corpus Money, Allowances, Compensations, Reimbursement of Fees of Consultants and other Expenses, Rent for

Temporary Alternative Accommodation and Deposits or any other form of receipt in the hands of the hands of the Society/ its individual members.

Ans. As per the Income Tax Act, 1961, no TDS is to be deducted on the amount reimbursed by the Developer to the Society or the Individual Members or on other items such as Corpus Money, Allowances, Compensations, Reimbursement of Fees of Consultants and other Expenses, Rent for Temporary Alternative Accommodation and Deposits or any other form of receipt.

However, when the Society makes payments such as Professional Fees, Contractor, etc, the Society is to Deduct Tax at Source at the rate specified in act and pay the same to the Income Tax Department and file the Quarterly Returns:

IX] Responsibility/ Liability towards stamp duty.

Responsibility/Liability of the Society/its individual members towards Stamp Duty, if any, in transition from surrender of existing premises to the Develop to the occupation and registration of the Redeveloped premises

Ans. Normally, in the cases of Redevelopment, the Stamp Duty and the Registration Charges on surrender of the existing premises to the Developer for the purpose of Redevelopment would be paid by the Developer.

Whereas, when the Individual Members receives the Redeveloped Premises from the Developer, he is liable to pay Stamp Duty and Registration Charges on the same. The Stamp Duty payable would be on the cost of construction of the present area of the Premises and on the market value for the extra area received as per the Ready Reckoner Value published by the Government of Maharashtra every year on 1st January.

XII] Restructuring of Society.

Whether the composition of the Society may need to be restructured in any manner so as to facilitate minimization of the tax liability.

Whether admission of new members (from saleable portion) in the existing Society or their Accommodation as an independent new Society would have any bearing on the tax liability of the Society/its individual members.

Ans. No, the composition of the Society need not be restructured in any manner so as to facilitate minimization of the tax liability.

The admission of the new members to the existing Society or their accommodation to the new Society would not make much difference to the tax liability of the Society or its Individual Members.

However, it would be advisable to admit the new members to the existing Society because due to increase in the number of the Members of the Society, the fixed charges or expenses of the Society like maintenance, etc would be distributed amongst the Members.

9. JOINT DEVELOPERMENT AND TAXATION:-

a) Problem:-

In metro cities concept of joint development is in boom, because due to hiked in price and various complexities involve in immovable property and their title issue. Under this arrangement consideration mostly settled on sharing basis. But, the main issue arises in hands of land owner. Because as per earlier provisions of section 45, capital gain is chargeable to tax in the year in which transfer takes place. The definition of 'transfer', inter alia, includes any arrangement or transaction where any rights are handed over in execution of part performance of contract, even though the legal title has not been transferred.

In such a scenario, execution of Joint Development Agreement between the owner of immovable property and the developer triggers the capital gains tax liability in the hands of the owner in the year in which the possession of immovable property is handed over to the developer for development of a project due to trigger of Section 53A of Transfer of Property Act, 1882 in spite of the fact that the consideration thereof (i.e. the actual constructed property) will be received only after a couple of years. But, as the land owner will get the constructed portion in lieu of transfer of development right. So, at the time of capital gain land owner has to pay capital gain from his own pocket by deploying actual his own funds. This created huge financial hardship on land owner.

Further, litigation around characterization of income, timing of taxation of capital gains, determination of sale consideration etc. are is aggravating the assessee's concerns.

b) Solution

To minimise the genuine hardship of land owners new sub-section (5A) in section 45 so as to provide that in case of an assessee being individual or Hindu undivided family, who enters into a registered agreement for development of a project on his land or building or both and in lieu of that he receive share in such project with or without some consideration received in monetary consideration, the capital gains shall be chargeable in the year in which the certificate of completion for the whole or part of the project is issued by the competent authority.

c) How to compute

The stamp duty value of land owner share as on the date of issuing of certificate of completion as increased by any monetary consideration received, if any.

d) Conditions

i) From Land Owner Point of View

Landowner cannot transfer his share in the project to any other person on or before the date of issue of certificate of completion. If he transfers then, the capital gains will be taxable in the year in which he transfer his share.

ii) From Developer Point of View

As section 194-IC if any monetary consideration is payable under the specified agreement covered under sub-section 5A of section 45 that, tax at the rate of ten per cent shall be deductible from such payment.

e) Issue remains:-

Sub-section 5A of section 45 only covered those transactions which are entered by land owner who are individual or HUF. If land owner is differed from Individual or HUF then tax liability will arise in the year when possession was handed over for development of project.

10. TAX AUDIT

Amount received as advance by builder following project completion method whether tax audit applicable and penalty under section 271B imposable

In case it is taken that assessee is following the system in which income is returned on completion of the project and in case project goes on for more than 5 years and assessee gets its books of account audited for last year in which project is completed, then from where A.O. will be able to verify the figures of expenses and receipts etc. of earlier years. So, it is against the very principle of Section 44AB that in project completion assessee would get the books of account audited in the last year and not in earlier years when he is debiting the expenses and showing sundry debits and different types of receipts are also there. On the basis of above, it can be concluded that audit is to be carried on for all the assessment years during which the project was constructed and the expenses were debited to the P & L A/c.

It is held that amounts received as advance by the assessee-builder from customers had an element of profit and same were to be adjusted towards the cost of flats booked by each customer and thus, the amounts of advance have to be included in "gross receipts" for the purpose of s. 44AB; assessee being under obligation to get its accounts audited under s. 44AB. It cannot be contended that the assessee following project completion method would get the books of account audited in the last year and not in earlier years when he is debiting the expenses and other items and showing different types of receipts penalty under s. 271B was imposable for its failure to get the same done

Gopal Krishan Builders [2006] 92 TTJ 215 (Luck)]

11. Real Estate Transaction and Stamp Duty Valuation:-

i) Buyer Point of View:-

It was seen in past that real estate transaction involved black money because transactions are registered at undervalued consideration. To overcome with this situation provision u/s 56(2)(vii)(b) was introduced. So, if any buyer purchases any immovable property below the stamp duty value and difference in value is 50000 then difference amount will be taxable in hands of buyer. However, above provision was restricted to Individual and HUF buyer who purchase immovable property for their investment or personal purpose. Thus, to overcome with this inequality legislature introduce provision of section 56(2)(x) was introduced and all assesse gets covered in this provision. So, currently none of the assesse can purchase any property below the stamp duty value. Otherwise difference amount will be taxable in buyer.

ii) Seller Point of View:-

Legislature introduces same analogy in hands of Seller also. If seller offers income under capital gain head, then provision of section 50C will come into picture and sale consideration will be substituted from stamp duty value. Similarly of he offered income

under business head in that situation also provision of section 43CA will come and it will substitute actual sale consideration from stamp duty valuation.

12. CAPITAL GAIN

12.1 CAPITAL ASSET

Capital asset means any property of any kind held by an assessee, whether or not connected with his business or profession

However, agricultural land in India is not a capital asset provided it is not situated:-

a) *In any* ***area which is comprised within the jurisdiction of a municipality*** *(whether known as municipality, municipal corporation, notified area committee, town area committee, town committee, or by any other name) or a cantonment board* ***and which has a population of not less than ten thousand*** *[according to the last preceding census of which the relevant figures have been published before the first day of the previous year];* ***or***

b) *In any area within the distance, measured* ***aerially,***-

   (I) *Not being more than two kilometers, from the local limits of any municipality or cantonment board referred to in item (a) and which has a population of more than ten thousand but not exceeding one lakh; or*

   (II) ***Not being more than six kilometers****, from the local limits of any municipality or cantonment board referred to in item (a) and which has a population of more than one lakh* ***but not exceeding ten lakh****; or*

   (III) *Not being more than eight kilometers, from the local limits of any municipality or cantonment board referred to in item (a) and which has a population of more than ten lakh.*

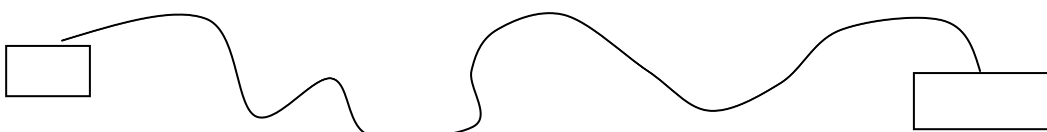
As the clause of section 2(14)(iii) start with **"Not being land situated"**. Therefore, if land is situated within that area then land will be classified as "urban agricultural land". Distance from jurisdiction or municipality or cantonment board within which agricultural land is to be located for it to be considered as urban land depending on the population of the municipality or cantonment boards which is as under:-

Distance	**Population**
Within 2 kilometers	10,000-1,00,000
2 kilometers – 6 kilometers	1,00,000-10,00,000
6 kilometers – 8 kilometers	More than 10,00,000

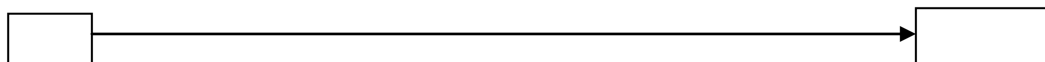
The distance from the Municipal Corporation measurement:

Such distance is to be measured on **straight line aerially** as crow flies. The shortest aerial distance has to be considered. Such shortest aerial distance is defined as "A straight line distance between two places." A human would travel further to get from one point to another due to obstacles or lack of roads or trails, but a crow can go in a straight line between them. Humans have to follow roads which have their twists and turns. But, a crow does not have to face the barriers that humans face. Hence, we measure the straight line distance between two places.

Human By road



Crow's flight straight line distance (aerial measurement)



<u>Analysis of section in present situation:</u>

Agricultural land in nature of urban land is liable for tax. But, if querist land not satisfies any of the criteria of urban agricultural land mentioned below, then it will be treated as rural agricultural land and will not be taxable.

Clause	*Condition for being urban agricultural land*	*Simple Words*
(a)	*Land should be in jurisdiction of municipality* ***and*** *area where land is situated, that area population must be more than 10000*	*Act provides twin condition i.e. it should be within jurisdiction of municipality & population of area must be more than 10000. As <u>AND</u> word has mention in condition, so both conditions require to be satisfy.*
(b)(I)	*Land should be situated within 2 kms of any municipality having population more than 10,000 but less than 1,00,000*	*Act provides twin condition i.e. it should be within 2 KMS of any municipality & population of that municipality must be more than 10000 but less than 100000. As <u>AND</u> word has mention in condition, so both conditions require to be satisfy.*
(b)(II)	*Land should be situated within 6 kms of any municipality having population more than 100,000 but less than 10,00,000*	*Act provides twin condition i.e. it should be within 6 KMS of any municipality & population of that municipality must be more than 100000 but less than 1000000. As <u>AND</u> word has mention in condition, so both conditions require to be satisfy.*
(b)(III)	*Land should be situated within 8 kms of any municipality having population more than 10,00,000*	*Act provides twin condition i.e. it should be within 8 KMS of any municipality & population of that municipality must be more than 1000000. As <u>AND</u> word has mention in condition, so both conditions require to be satisfy.*

<u>Note:</u> In order to qualify for agricultural land in India, it is not necessary that the land was once agricultural land. It must be an agricultural land at the time of sale. In order to determine whether a particular land is agricultural land or not, it is first necessary to ascertain what is the use to which the land is been actually put. If it is been used for agricultural purposes or even if the agricultural use has ceased but it is apparent that the land is meant to be used for agricultural purpose, it would be an agricultural land.
Ranchhodbhai Bhaijibhai Patel V. Cit (1971) 81 Itr 446 (Guj.)

12.2 TRANSFER IS A PRE-REQUISITE FOR TAXING CAPITAL GAIN

Capital gain arises only when there is a *transfer* of capital asset. If the capital asset is not transferred or if there is any transaction which is not regarded as transfer, there will not be

any capital gain. However w.e.f. assessment year 2000-2001 section 45(1A) has been inserted to provide that in case of profits or gains from insurance claim due to damage or destruction of property, there will be capital gain on such deemed transfer although no asset has been actually transferred in such case.

12.3 HOLDING PERIOD OF IMMOVABLE PROPERTY

(A) Short-term capital asset (Immovable): A capital asset held by an assessee for not more than 24 months *immediately preceding the date of its transfer* is known as a short term capital asset.

(B) Long-term capital asset: It means a capital asset which is not a short-term capital asset. In other words, if the asset is held by the assessee for more than 24 months, such an asset will be treated as a long-term capital asset.

Thus, period of holding of a capital asset is relevant for determining whether capital asset is short-term or long-term.

Exclusion/inclusion of certain period for computing the period of holding of an asset:

Case	*Exclusion/Inclusion of period*
Property acquired in any mode given under section 49(1) (*e.g.* by way of gift will, etc.)	Include the holding period of previous owner also.

Judicial decisions for determining period of holding

i) *Property constructed on a land purchased earlier*: In case of property is constructed on a site purchased much earlier, the question arises whether the period of holding the asset *i.e.*, the property, should be reckoned from the date of completion of the construction of the property or from the date of acquisition of the land.

The correct position is that the asset consists of two components: (1) Land and (2) Building. When the property is sold, the period of holding has to be reckoned separately for the land and the building. The consideration received can also be split into two parts relating to each component.

*In **CIT v Vimal Chand Golecha (1993) 201 ITR 442 (Raj)**, the land was purchased in 1962 and building was constructed thereon in the accounting years relevant to assessment years 1968-69, 1969-70 and 1970-71. The building was sold in 1970. It was held that the gains attributable to land were assessable as long-term capital gains. The gains attributed to the building were however, short-term capital gains. Similar decision was held in the cases of **CIT v Lakshmi B. Menon (2003) 264 ITR 76 (Ker) and CIT v C.R. Subramanian (2000) 242 ITR 342 (Kar)**.*

Agreeing with the above Rajasthan High Court view, it has been held that land can be considered a separate capital asset even if a building is constructed thereon. Thus, where the land is held for more than a prescribed period, the gains arising from the sale of the land can be considered as long-term capital gains even though the building thereon, being a new construction, is held for a period less than the prescribed one

CIT v Dr. D.L. Ramachandra Rao (1999) 236 ITR 51 (Mad)
CIT v Citibank N.A. (2004) 260 ITR 570 (Bom)

CIT v Estate of Omprakash Jhunjhunwala (2002) 254 ITR 152 (Cal)
Period of holding of share in the co-operative housing society: *While computing the capital gain tax in case of transfer of his shares by a person who is a member of cooperative housing society, the relevant date would be date on which the member acquires the shares in the cooperative housing society and the date on which member had sold his shares therein. Thus, where the assessee acquired shares in the society on 6-9-1979 and was allotted flat on 15-11-1979. He was given possession of flat in October 1981, and sold the shares of the society along with the flat, on 4-12-1982, the capital gains arising from the sale were long term capital gains, shares having been held for more than 36 months.*
CIT v Anilben Upendra Shah (2003) 262 ITR 657 (Guj)

Similarly, the assessee became a member in Venus Apartments (Galaxy Co-operative Housing Society). He was allotted a flat in the building of the society by resolution dated 4-11-1980, passed by the managing committee of the society. On the date of allotment, i.e., 4-11-1980, the property was under construction and came to be completed on 12-9-1983. Physical possession was handed over to the assessee on 12-9-1983. On 30-4-1984, the flat was sold by the assessee for a consideration of Rs. 3,75,000. The assessee worked out long-term capital gains at Rs. 1,59,395. The Assessing Officer did not accept the stand of the assessee that the assessee had become the owner of the property as per resolution dated 4-11-1980.

According to the AO the assessee had held the property for a period of less than 36 months and as such was liable to short-term capital gains tax, it was held that the assessee in the present case was allotted a share by the co-operative housing society on 4-11-1980, and the sale of the same took place on 30-4-1984, i.e., after a period of 36 months. The Tribunal was therefore justified in holding that the capital gains arising were long-term capital gains and the assessee was entitled to deduction from such gains as per law.
CIT v Jindas Panchand Gandhi (2005) 279 ITR 552 (Guj)
Right to acquire any house property: Where a flat is booked with a builder under a letter of allotment or an agreement for sale, this would represent only a right to acquire a flat and if such right is acquired more than 36 months back, it becomes a long-term asset. However, when the possession of the flat is taken, the period of holding would once again commence from the date of the possession of the flat as the small right to acquire a flat merged into larger right and small right upon a merger would loose its existence.

12.4 COST OF ACQUISITION

Cost of acquisition of an asset is the value for which it was acquired by the assessee. Expenses of capital nature for completing or acquiring the title of the property are includable in the cost of acquisition.

Judicial decision on cost of acquisition:

Cost of acquisition of an asset acquired from the previous owner in any mode given u/s 49(1): In this case, the cost of acquisition is taken as the cost to the previous owner and it is this cost which will have to be indexed. For the purpose of indexation the year in which the asset was *first held* by the assessee (not the previous owner) is to be considered. The indexation will be done as under:

Cost of acquisition to the previous owner × **Fehler!**

However, in the case of *Mrs.* ***Pushpa Sofat*** **(2002) 81 ITD 1 (Chd)(SMC),** the indexation of cost was allowed from the date of acquisition of the asset by the previous owner and not the date when the asset was acquired by the assessee from the previous owner under any mode given under section 49(1).

12.5 VALUATION AS ON 1.4.2001

From AY 2018-19 base year for taking fair value and indexation benefit thereon shifted to 2001. So, now the assesse who have capital asset (Other than goodwill of a business or a right to manufacture, produce or process any article or thing or right to carry on any business or profession) which are purchase between 1.4.1981 to 31.03.2001 can take benefit of substitution of actual cost of acquisition by fair value as on 1.4.2001.

13. EXEMPTION OF CAPITAL GAINS UNDER VARIOUS SUB-CLAUSES OF SECTION 10, SECTION 11(1A) AND SECTION 13A

Exemption of capital gains on compensation received on compulsory acquisition of agricultural land situated within specified urban limits:

With a view to mitigate the hardship faced by the farmers whose agricultural land situated in specified urban limits has been *compulsorily acquired,* the Finance (No. 2) Act, 2004 has inserted a new clause (37) in section 10 so as to exempt the capital gains (whether short-term or long-term) arising to an *individual or a Hindu undivided family* from transfer of agricultural land by way of *compulsory acquisition* where the compensation or the enhanced compensation or consideration, as the case may be, is received *on or after 1-4-2004*.

The exemption is available only when such land has been used for agricultural purposes during the preceding two years *by such individual* or a *parent of his* or by *such* Hindu undivided family.

Where the compulsory acquisition has taken place before 1-4-2004 but the compensation is received after 31-3-2004, it shall be exempt. But if part of the original compensation in the above case has already been received before 1-4-2004, then exemption shall not be available even though balance original compensation is received after 31-3-2004.

However, enhanced compensation received on or after 1-4-2004 against agricultural land compulsory acquired before 1-4-2004 shall be exempt.

14. EXEMPTION OF CAPITAL GAINS U/s. 54, 54B, 54EC & 54F

a) *Profit on transfer of house property used for residence [Section 54]*:

Benefit of section 54 is confined to sale of a residential house after 24 months and reinvestment in a residential house. Reinvestment benefits are available both for purchase and construction of the house. Purchase has to be either one year before or two years later. Construction has to be completed within three years of the sale of the asset in respect of which benefit of reinvestment is claimed. There have been many decisions on purchase/construction of the house. Further, certain clarifications have also been issued in this regard. These have been summarized as under:

i. *House includes part of the house*: House property does not mean a complete independent house. It includes independent residential units also, like flats in a multi-storeyed complex. The emphasis is not on the type of the property, but, on the head under which the rental income is assessed. [*CIT* (*Addl.*) v *Vidya Prakash Talwar* (1981) 132 ITR 661 (Del)].

ii. *Release deed may also be treated as purchase*: Where a property is owned by more than one person and the other co-owner or co-owners release his or their respective share or interest in the property in favour of one of the co-owners, it can be said that the property has been purchased by the releasee. Such release also fulfils the condition of section 54 as to purchase so far as releasee-assessee is concerned [*CIT* v *T.N. Aravinda Reddy* (1979) 120 ITR 46 (SC)]

iii. *Addition of floor to the existing house eligible for exemption under section 54*: The assessee sold his residential property and invested the capital gain within the stipulated time in the construction of a new floor on another house owned by him by demolishing the existing floor, it was held that he was entitled to exemption under section 54. [*CIT* v *Narasimhan* (*PV*) (1990) 181 ITR 101 (Mad)].

iv. *No exemption under section 54 if land only is sold*: The house property concerned must be building or land appurtenant to building. The basic test was whether the land appurtenant to building could be used independent of the user of the building. If so, it cannot be said to be land appurtenant to building. Further, the basic requirement is that the capital gain should arise from the transfer of building or land, the income of which is chargeable under the head Income from house property. If the land alone is sold, the provisions of section 54 will have no application inasmuch as the income from land is not chargeable under the head Income from house property. [*CIT* v *Zaibunnisa Begum* (1985) 151 ITR 320 (AP)].

v. *Successor is entitled to benefit of exemption in case of death of the assessee*: In case of assessee's death during the stipulated period, benefit of exemption under section 54(1) is available to legal representative if the required conditions are satisfied by the legal representative. [*Ramanathan* (*CV*) v *CIT* (1980) 155 ITR 191 (Mad)].

vi. *Purchase of limited interest in the house eligible for exemption under section 54*: Where an

assessee had sold the residential house and acquired only 15% interest in another house and such other house was already used for residence prior to purchase, it was held that the benefit should be available to the assessee. [*CIT* v *Chandaben Maganlal* (2000) 245 ITR 182 (Guj)]. In coming to the conclusion, the High Court followed its own earlier decision in *CIT* v *Tikyomal Jasanmal* (1971) 82 ITR 95 (Guj). In that case, what was purchased was a unit of house property, while in the present case before the High Court, it was a limited interest in the property.

vii. *Construction in another property not eligible for exemption*: An assessee gifted some land to his wife. He, thereafter constructed a building on the said land. The Government acquired the land and building and paid compensation for land to the wife and for the building to the assessee (husband). It was held that capital gain on land was assessable in the hands of the husband by virtue of section 64 but he was not entitled to exemption under section 54 in respect of capital gain on the acquisition of the land of the wife as the capital gain to the wife did not arise on transfer of a residential house. [*T.N. Vasavan* v *CIT* (1992) 197 ITR 163 (Ker)].

viii. *House of the firm used by partners*: Where a firm's property is used for residence of partners and thereafter distributed to the partners upon dissolution of the firm and the partner sells the same, exemption can be claimed by the partner under section 54. For this purpose, period for which this property was held by the firm shall also be taken into account for determining the question whether the house property in exemption was a long-term capital asset or not. [*CIT* v *M.K. Chandrakanth* (2002) 258 ITR 14 (Mad)].

ix. *There can be both purchase and construction*: Where the assessee had partly invested the capital gains on the purchase of another house and partly on the construction of additional floor to the house so purchased within the prescribed time limit, it was held that the Income-tax Officer was not justified in restricting exemption to investment on purchase only, holding that the exemption u/s 54 was admissible either for purchase or for construction but not for both. [*Sarkar* (*B.B.*) v *CIT* (1981) 132 ITR 661 (Del).

x. *Construction can start before the sale of asset*: The construction of the new house may start before the date of transfer, but it should be completed after the date of transfer of the original house. [*CIT* v *J.R. Subramanya Bhat* (1987) 165 ITR 571 (Karn)]. The very fact that purchase of another house as also the construction can take place before the sale means that cost of purchase or new construction need not flow from the sale proceeds of the old property. [*CIT* v *H.K. Kapoor* (*Decd*) 1998 234 ITR 753 (All) and *CIT* v *M. Vasudevan Chettiar* (1998) 234 ITR 705 (Mad)].

xi. Allotment of a flat by DDA under the Self-Financing Scheme shall be treated as construction of the house [Circular No. 471, dated 15-10-1986]. Similarly, allotment of a flat or a house by a cooperative society, of which the assessee is the member, is also treated as construction of the house

[Circular No. 672, dated 16-12-1993]. Further, in these cases, the assessee shall be entitled to claim exemption in respect of capital gains even though the construction is not completed within the statutory time limit. [*Sashi Varma* v *CIT* (1997) 224 ITR 106 (MP)]. Delhi High Court has applied the same analogy where the assessee made substantial payment within the prescribed time and thus acquired substantial domain over the property, although the builder failed to hand over the possession within the stipulated period. [*CIT* v *R.C. Sood* (2000) 108 Taxman 227 (Del)].

xii. As per a circular of CBDT, the cost of the land is an integral part of the cost of the residential house, whether purchased or constructed. [Circular No. 667, dated 18-10-1993].

xiii. Where an assessee who owned a house property, sold the same and purchased another property in the name of his wife, exemption under section 54 shall be allowable. **[*CIT* v *V. Natarajan* (2006) 154 Taxman 399 (Mad)]**.

xiv. Where the assessee utilized the sale consideration for other purposes and borrowed the money for the purpose of purchasing the residential house property to claim exemption under section 54, it was held that the contention that the same amount should have been utilised for the acquisition of new asset could not be accepted. [*Bombay Housing Corporation* v *Asst. CIT* (2002) 81 ITD 454 (Bom). **Also** followed in ***Mrs. Prema P. Shah, Sanjiv P. Shah* v *ITO* (2006) 282 ITR (AT) 211 (Mumbai)**].

b) *Capital gain on transfer of land used for agricultural purposes [Section 54B]*:

Any capital gain (short-term or long-term), arising to an assessee (only individuals), from the transfer of any agricultural land which has been used by the assessee or his parents for at least a period of 2 years immediately preceding the date of transfer, for agricultural purposes, shall be exempt to the extent such capital gain is invested in the purchase of another agricultural land within a period of 2 years after the date of transfer to be used for agricultural purpose, provided the new agricultural land purchased, is not transferred within a period of 3 years from the date of its acquisition.
Section 54B is applicable only to individuals and not to any other assessee this is because the section uses the expression used by "his or a parent of his" which clearly indicate that the "assessee" refers to an individual. [*CIT* v *Devarajalu* (*G.K.*) (1991) 191 ITR 211 (Mad)].

c) *Capital gain on transfer of long-term capital assets not to be charged on investment in certain bonds [Section 54EC]*:

Any long-term capital gain, arising to any assessee, from the transfer of any capital asset on or after 1-4-2000 shall be exempt to the extent such capital gain is invested within a period of 6 months after the date of such transfer in the long-term specified asset provided such specified asset is not transferred or converted into money within a period of 3 years from the date of its acquisition. The maximum permissible deduction against capital asset is same

financial year or/and subsequent financial year cannot exceed 50 lakh.

Exemption under section 54EC not available in respect of deemed capital gains on amount received on liquidation of a company: Section 54E (now section 54EC) permits reinvestment benefit, if the sale proceeds/capital gains on sale of long-term capital assets are invested in the manner required by the section. Where a shareholder is made liable for deemed capital gains on amount received on liquidation of a company, is he eligible for reinvestment benefit under section 54E (now 54EC)? It was held that section 54E (now 54EC) would have application only where there is an actual transfer and not in a case, where there is only a deemed transfer. [*CIT* v *Ruby Trading Co. Pvt. Ltd.* (2003) 259 ITR 54 (Raj)].

Benefit under section 54EC, etc. available even on transfer of depreciable assets: Although as per section 50 the profit arising from the transfer of depreciable asset shall be a gain arising from the transfer of short term capital asset, hence short-term capital gain but section 50 nowhere says that depreciable asset shall be treated as short-term capital asset. Section 54E [or say 54EC or 54F, etc.] is in independent provision which is not controlled by section 50. If the conditions necessary under section 54E are compiled by the assessee, he will be entitled to the benefit envisaged in section 54E, even on transfer of depreciable assets held for more than 36 months. [*CIT* v *Assam Petroleum Industries* (*P.*) *Ltd.* (2003) 131 Taxman 699 (Gau). See also *CIT* v *ACE Builders Pvt. Ltd.* (2005) 144 Taxman 855 (Bom)].

On the same analogy benefit under section 54EC or 54F shall be available in the case of depreciate asset if these are held for more than 36 months.

d) *Capital Gain on transfer of asset, other than a residential house [Section 54F]*:

Any long-term capital gain, arising to an individual or HUF, from the transfer of any capital asset, *other than residential house property*, shall be exempt in full, if the entire net sales consideration is invested in purchase of one residential house within one year *before* or two years *after* the date of transfer of such an asset or in the construction of one residential house within three years after the date of such transfer. Where part of the net sales consideration is invested, it will be exempt proportionately.

The above exemption shall be available only when the assessee does not own *more than one residential* house property *on the date of transfer* of such asset exclusive of the one which he has bought for claiming exemption under section 54F.

Section 54 and 54F are comparable in many respects. Hence, the law and precedents relating to section 54 as to whether the house property on which investment is made is residential or not, the law relating to time limits, the precedent that construction could start earlier though completed within three years are all equally applicable for section 54F. Hence, for judicial decisions for section 54F, refer to the judicial decisions given under section 54.

15. <u>CAPITAL GAIN ON THE TRANSFER OF LAND, FORMING PART OF BUILDING WHICH IS DEPRECIABLE, CAN BE LONG-TERM</u>

Section 50 provides for determination of the cost of construction of superstructure and it does not apply to land as land is not a depreciable asset. Hence, if the building comprising of the land is sold, the capital gain on superstructure shall be short-term capital gain in terms of section 50 and the capital gain on land, if held for more than 36 months (Now 24 months), shall be long-term capital gain. This is because the land is independent and identifiable capital asset and it continues to remain so even after construction of the building thereon. [*CIT* v *CITI Bank NA* (2003) 261 ITR 570 (Bom)].

16. <u>BLOCK OF ASSETS – SECTION 2(11).</u>

Where land and building were used for the business, an important issue arises whether the new constructed area received can be added to the block of assets. The new constructed area will not be a building used for the purpose of the business. If it is not an asset which will be used as a "Building" for the purpose of business, it may not become a part of the Block of Assets.

For the purpose of redevelopment, the old building has to be demolished. Such building may be part of the block of asset. Issue arises as to whether indexed cost of structure can be deducted to arrive at the long term capital gains on the sale of land. Indexation u/s. 48 is allowed only in respect of cost of acquisition or cost of improvement of the capital asset transferred. Therefore, one may contend that only the land is transferred and not the building, which will be demolished to enable the development of land, hence the cost of structure cannot be taken into consideration and only index cost of land will be considered.

17. <u>TDS ON PURCHASE OF IMMOVABLE PROPERTY:-</u>

Under Section 195, on transfer of immoveable property by a non-resident, tax is required to be deducted at source by the transferee. However, there is no such requirement on transfer of immoveable property by a resident except in case of compulsory acquisition of certain immoveable properties (section 194LA).
The Finance Act, 2013 inserted new section 194-IA to introduce TDS on consideration on transfer of immoveable properties.

The objects of this have been explained by Explanatory Memorandum as under:
"*There is a statutory requirement under section 139A of the Income Tax Act read with rule 114B of the Income Tax Rules 1961 to quote Permanent Account Number (PAN) in documents pertaining to purchase or sale of immoveable property for value of Rs.5 lakh or more. However, the information furnished to the department in Annual Information Returns by the Registrar or Sub-Registrar indicate that a majority of the purchasers or sellers of immoveable properties, valued at Rs.30 lakhs or more, during the financial years 2011-2012 did not quite or quoted invalid PAN in the documents relating to transfer of property. In order to have a reporting mechanism of transaction in the real estate sector and also to collect tax at the earliest point of time, it is proposed to insert a new section 194-IA…*"

The Finance Minister in his speech explained the objects of the new section 194-IA as under:

"145. Transactions in immoveable properties are usually under valued and under reported. One-half of the transactions do not carry the PAN of the parties concerned. With a view to improve the reporting of such transactions and the taxation of capital gains, I propose to apply TDS at the rate of one percent on the value of transfer of immoveable property where the consideration exceeds Rs.50 lakhs. However, agricultural land will be exempt."

Section 194-IA provides that every transferee (purchaser or buyer), at the time of making payment or crediting of any sum as consideration for transfer of immoveable property (other than agricultural land) to a resident transferor, shall deduct tax, at the rate of 1% of such sum. In order to reduce the compliance burden on small taxpayers, no deduction of tax shall be made where the total amount of consideration for the transfer of an immoveable property is less than Rs.50, 00,000. The provisions of section 203A [regarding obligation of deductors to obtaining tax deduction and collection account number (i.e. TAN) shall not apply in respect of tax deducted under this section. This amendment will take effect from 01.06.2013.

18. DEDUCTION U/S 80IBA:-

SN	*CONDITION*	*REMARK*
1	*Project must be approved by competent authority after 01-06-2016 but on or before 31-03-2019*	*If approval for housing project is obtained more than once, than the date of first approval should be taken as the date of approval of the project.* *Like first plan approved on 30.03.2017 & amended project plan approved on 20.08.2017, then the date of approval will be taken as 30.03.2017.*
2	*The project must be completed within a period of Five years from the date of approval by the competent authority*	*Date of completion of project will be the date when the completion certificate issued by the competent authority in writing for the entire project.* *If the project not completed within the statutory permissible time, the in the year of expiry of such period all the year years deduction claimed in respect of the housing project will be treated as the income of the that previous year.*
3	*Shops and commercial built up area cannot exceed 3% of total carpet area of the project.*	
4	*Land area of project cannot be less than 1000 sq. mtr in metro cities and 2000 Sq Meters in other area.*	
5	*Carpet area of residential unit of housing project will not be exceed 30 sq. mtr in 4 metro cities and 60 Sq Meter (645.83 Sq Feet) in other area.*	*"Carpet area" shall have the same meaning as assigned to it in clause (k) of section 2 of the Real Estate (Regulation and Development) Act, 2016 (16 of 2016)*

		i.e. *the net usable floor area of an apartment, excluding the area covered by the external walls, areas under services shafts, exclusive balcony or verandah area and exclusive open terrace area, but includes the area covered by the internal partition walls of the apartment.* *Explanation.-- For the purpose of this clause, the expression "exclusive balcony or verandah area" means the area of the balcony or verandah, as the case may be, which is appurtenant to the net usable floor area of an apartment, meant for the exclusive use of the allottee; and "exclusive open terrace area" means the area of open terrace which is appurtenant to the net usable floor area of an apartment, meant for the exclusive use of the allottee;*
7	*If an individual is allotted a residential unit in the project, no other unit should be allotted to the;* *a) same individual* *b) spouse of the individual* *c) minor children of such individual*	
8	*Project should utilise the Floor Area Ratio not less than 90% in four metro cities and 80% in other area*	"floor area ratio" means the quotient obtained by dividing the total covered area of plinth area on all the floors by the area of the plot of land.
9	*Separate books to be maintained for such project*	
10	*Project should be taken in own capacity (i.e. risk & reward of the assesse and not perform activity in capacity of contractor.*	

If the real estate developer comply all of the above condition, they will get 100% deduction of profit earn from that housing project.

19. <u>115JB & 115JC and Deduction u/s 80IBA:-</u>

Entities who are claiming deduction u/s 80IBA are require to pay tax under section 115JB (in case of company) or u/s 115JC (other than company), because under 115JB deduction u/s 80IBA cannot be deducted from book profit and under 115JC we need to add back deduction u/s 80IBA. Therefore, even entities are claiming deduction under normal income tax provision. But, same time they need to pay MAT/AMT on deduction claimed u/s 80IBA.

THANK YOU