FICCI Budget Recommendations (2021-22)

HOUSING & REAL ESTATE

DIRECT TAX

1 Align draft ICDS for real estate developers with IND-AS 115

CBDT has clarified in the FAQ issued on March 23, 2017, vide Circular No 10/2017 that ICDS IV is not applicable to real estate developers**.** Nonetheless, Finance Act, 2018 inserted section 43CB in the Act to bring certainty on the applicability of ICDS. The draft ICDS on Real Estate Transactions provides for the application of the Percentage of Completion Method when:

a) the expenditure incurred on construction and development costs is 25 % or more of the construction and development costs;

b) 25% or more of the saleable project area is secured by contracts or agreements with buyers; and

c) 10% or more of the total revenue as per the agreements of sale or any other legally enforceable documents are realized in respect of each of the contracts and it is reasonably certain that the parties to such contracts will comply with the payment terms as defined in the contracts.

As the draft ICDS provides for the percentage of completion method, this gap between the Notification issued by the MCA and the aforesaid draft ICDS is required to be bridged by bringing clarity on applicability of ICDS for real estate developers by modifying the draft ICDS appropriately to include project completion method as one of the methods to recognize revenue and thereafter issuing the final ICDS.

It may be noted that non-alignment of the proposed ICDS to be notified for real estate developers with the applicable Ind-AS 115 will cause undue hardship on the taxpayers of the real estate sector, as they would be forced to maintain two separate set of books of accounts – one for preparation of financial statements as statutorily required as per Ind-AS 115 following the project completion method for revenue recognition and the other set of financial statements for computing taxable income based on the proposed ICDS for real estate transactions which currently prescribes the Percentage of Completion Method (POCM) for revenue recognition.

It is recommended that draft ICDS for real estate developers should be modified to bring it in line with the revenue recognition principle as per IND AS 115.

2 Provision regarding taxation of unsold property on notional basis should be withdrawn with retrospective effect or at least amend the Section 23 of the Act to tax the deemed income only when the property is developed as rent income generating assets

Section 23(5) of the Act provide the manner of determination of annual value of house property held as stock-in-trade. The annual value of such property for the period up to two years from the end of the financial year in which the certificate of completion of construction of the property is obtained from the competent authority, is taken to be nil. It is a known fact that various developers have not been able to sell their stock even after the certificate of completion is received due to various business exigencies and various macro-economic factors. Also, the question of whether any notional income from house property held as stock-in-trade and not let out during the whole or any part of the previous year is taxable in the hands of the developer is open to litigation and the matter is currently *sub-judiced* before the Hon'ble Supreme Court.

The application of this section leads to an extremely prejudicial treatment for the real estate developers as they have stock which they are unable to sell leading to a funds crunch and on top of that they are required to shell out money for paying tax on the notional income. It is recommended that this section should be withdrawn to reduce the genuine hardship faced by the developers.

Real Estate developer assessee's held the land and building as inventory for development and sale to the consumers like any other manufacturer holds raw material, under process stock and finished goods. It is not possible for the real estate developers to lease out the ready to move inventory, hence taxing the deemed rental on the properties held for sale is highly unjustifiable. Further the sale of ready inventories are dependent on various factors and market conditions hence it may not be always possible to sale the entire inventory within 12 months of obtaining the occupation certificate.

It is recommended that the provision regarding taxation of unsold property on notional basis should be withdrawn with retrospective effect or at least amend Section 23 of the Act to tax the deemed income only when the property is developed as rent income generating assets (investment property as per IND-AS 40).

3 Include Real Estate sector within the purview of Section 72A

As per Section 72A of the Act the benefit of carry forward of and setoff of accumulated losses and unabsorbed depreciation is allowed only in case of merger/amalgamation of the company owning the Industrial undertaking. As per the current definition, the construction of real estate is not qualified as Industrial Undertaking. It is recommended that Section 72A of the Act be amended to include real estate sector within its purview. This will enable the consolidation and consequential efficiency for the sector.

4 Benefit of section 45(5A) be extended to companies, firms, LLPs

The Finance Act, 2017 had inserted section 45(5A) in the Act to provide for computation of capital gains in case of joint development agreement. The intent for inserting section 45(5A) in the Act was to reduce genuine hardships faced by land-owners in paying the capital gains tax liability in the year in which the possession of immovable property is handed over to the developer for development of a project. Similar to individuals and HUF's, any other taxpayer (viz. Company, firms, LLPs co-operative societies etc.), who being a land-owner intends to enter into a JDA for development of property, would also be faced with similar hardships. It is accordingly recommended that suitable amendment be made in section 45(5A) of the Act to extend its applicability to other taxpayers also viz. companies, firms, LLP etc. Widening the applicability of such beneficial provisions to other taxpayers will give an impetus to enter into JDAs and thereby boost real estate sector.

Section 45(5A) of the Act provides that in case of an assessee being individual or Hindu undivided family, who enters into a specified agreement for development of a project, the capital gains shall be chargeable to income tax as income of the previous year in which the certificate of completion of the whole or part of the project is issued by the competent authority. In order to remove ambiguity, it needs to be clarified that capital gains for the landowner should trigger only in that year in which certificate of completion is issued for his share in the constructed property and liability should be restricted to that part of the project for which certificate of completion is issued. Further thereto, various real estate developers own the development rights in the land and do not actually own the land. Hence, to cover such transactions under 'specified agreement', the meaning of specified agreement should be extended to the assessee owning the rights in the land.

5 Remove Restriction on Set-off of Loss from House Property

The Finance Act, 2017 has inserted sub-section (3A) in section 71 of the Act to provide that loss from house property up to Rs. 2 lakhs only will be set-off against the income under other heads in the same financial year. Loss above Rs. 2 lakhs is eligible to be carried forward for a period of eight years and can be set-off against income from house property only. This provision contradicts with the intention of the government to incentivise housing sector and promote investment in real estate sector. This could act as a dampener for promoting investment in the Housing sector. The limitation provided by the Finance Act, 2017 limiting the set-off of loss of house property to the extent of Rs. 200000 should be removed or at least interest of commercial property should be excluded from the restriction provided in the provision.

6 Issues related to 80IBA of the Act

a. Exclude projects eligible for deduction under Section 80IAB from the purview of MAT

Eligible projects entitled for 100% deduction under section 80-IBA are subjected to payment of (MAT) Minimum Alternate Tax (AMT). Utilisation of this MAT / AMT credit in succeeding 10 years is very difficult as the law allows to set-off the accumulated MAT/AMT credits only to the extent of differential amount of regular tax and MAT/AMT payable in the respective years. It may take 8 to 10 years for a Taxpayer to utilise the accumulated MAT/AMT credit, which on a net present value basis is quite insignificant. Effectively, the Taxpayer ends up paying tax at approx. 21.34% despite the 100% deduction in the tax computation.

It is therefore suggested either to exclude profits from projects qualified under section 80-IBA from the ambit of MAT/AMT provisions or to reduce the MAT/AMT rate on such profits suitably.

b. Relax conditions for claiming deduction under Section 80IAB

- The limit on carpet area of shops and commercial establishments is restricted to 3% of the aggregate carpet area. If the carpet area of shops and commercial establishments based on the requirement of the relevant competent authority of the jurisdiction is more than the limit of 3% of the aggregate carpet area prescribed, then there is a difficulty in going ahead with the affordable housing project. It is suggested that the limit should be relaxed to the extent of the limit as per the relevant competitive authority of the jurisdiction.
- As per the extant provisions of Section 80-IBA, the project shall be deemed to have been completed when a certificate of completion of project as a whole is obtained in writing from the competent authority. In case of development of affordable housing project on a big parcel of land consisting of various buildings, it will be difficult to complete the entire project as a whole within a period of five years. Generally, such huge projects are divided in phases. In such case, the time period of completion for each phase should be five years. It is suggested that if there are different phases in the project, then the period of completion of five years should be based on the start of each phase.