

October 15, 2020

Ref. No. MCHI/PRES/20-21/033

To,
Shri Sanjeev Kumar (I.A.S.)
Commissioner of Sales Tax
Maharashtra State
GST Bhawan, Mazgaon.

Sub: Representation regarding key issues faced by real estate sector under GST

Respected Sir,

The Confederation of Real Estate Developers Associations of India ('CREDAI') is the apex body for private Real Estate developers in India. We represent various Real Estate developers spread across India.

The Real Estate Sector is a significant contributor to GDP, the 2nd largest creator of jobs after Agriculture and directly supports nearly 250 industries. The Sector was already struggling hard to grasp and adapt itself to the fundamental changes and reforms brought in by demonetization, RERA, GST, IBC and the ban on Subvention scheme. The Sector was also facing the subdued demand due to slowdown in the economy, unaffordable prices and the liquidity constraints. COVID 19 pandemic and the consequential all-round disruption of business activities have thus dealt almost a mortal blow to the Sector!

It is, therefore, imperative that the Sector is provided all the necessary support by the Government which would enable it to tide over these critical times and revive itself as soon as possible. Considering the fact that this Sector is one of the chief contributors to the GDP, the early revival of the Sector would also significantly accelerate the revival of the economy once normalcy returns.

Since "Goods and Services Tax" (GST) policy has a significant impact on the overall performance of the Sector, the relief measures suggested herein are being restricted to only GST Policy.

We hereby provide the core **issues** faced by the Sector and the **recommendations** which could be considered by your Good self.

1. Taxability of Transfer of Development Rights (TDR), Long Term Lease of Land & Sale of Development Rights Certificate (DRC).

- 1.1 **Transfer of Development Rights:** In the real estate industry, it is a common practice for landowner/s and developers to come together and develop a property. In such cases, instead of selling the land for monetary consideration, the landowner/s provide the developer with the rights in the FSI emanating from the land and the developer uses its expertise of construction/ development of the project

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- 1.2 Long Term Lease of Land: Land parcels in many parts of India are transferred to Developers on Long Lease Basis by Landowners including Government agencies, such as Development Authorities. Generally, Landowners allow the bidders a defined period to make the full payment of long-term lease premium. The land parcel is handed over by the Landowners after entering into a Long Lease Agreement with the Developers for a period of generally more than 30 years.
- 1.3 Development Rights Certificate (DRC): This is a commonly adopted method by the Government for compensating a landowner for acquisition of his land that is required by the Government for public purpose. Essentially, in lieu of the acquisition of the land, rights for constructing built-up area proportionate to the value of the land acquired is provided by the Government to the Landowners by way of a DRC. This DRC can be used (fully or partly) by the Landowners himself for constructing a building or can be freely transferred to any other Person / Developer. Further, the DRC effectively represents permission to construct a specified built-up area over and above the inherent FSI of the land as provided by the applicable development control regulations.
- 1.4 As explained above the transfer of land and the rights inherent to it are done in various forms such as Sale of Land, TDR, Long Term Lease of Land, assignment of an existing Lease of Land or Sale of DRC. All of the above are nothing but transactions akin to Sale of Ownership rights in the Land.
- 1.5 **Reference is** made to other allied laws wherein 'benefit' arising from the land has always been included within "land" or "immovable property". This includes:
 - Real Estate (Regulation and Development) Act, 2016 - "Immovable property" includes land, buildings, rights of ways, lights **or any other benefit arising out of land** and things attached to the earth or permanently fastened to anything which is attached to the earth, but not standing timber, standing crops or grass
 - General Clauses Act, 1987 - "Immovable property" shall include land, **benefits to arise out of land**, and things attached to the earth, or permanently fastened to anything attached to the earth
 - Land Acquisition Act, 1894 - The expression "land" includes **benefits to arise out of land**, and things attached to the earth or permanently fastened to anything attached to the earth.
 - Also, various judicial pronouncements have been made regarding benefits arising out of land and such decisions are in tandem with above acts. Few of the citations are:
 - ✓ Dlf Limited vs Gurgaon I, Chandigarh Bench of tribunal;
 - ✓ Bahadur & other Vs. Sikandar MANU/UP/0016/1905;
 - ✓ Ananda Behera Vs. State of Orissa AIR 1956 SC 17;
 - ✓ Smt Dropadi Devi Vs. Ram Das AIR 1974 All 473;
 - ✓ Sadoday Builders (P) Ltd Vs. Jt Charity MANU/MH/0791;
 - ✓ Chheda Housing Development Corpn Vs. Bibijan Shaikh 2007 (2) Bom CR 587
- 1.6 Vide Notification No. 4/2019 of Central Tax dated 29.03.2019, Transfer of Development Rights and Long Term Lease Premium (in case where residential apartments are being constructed on such land) is exempt in the hands of the Transferor. However, the Promoter/Developer of such project is to pay GST at the rate of 18% on the value of the Development Rights / Lease Premium (limited to 1% on the value of the apartment for affordable apartments & 5% for other than affordable apartments) remaining unsold at the time of issuance of occupancy certificate or first occupation under reverse charge.
- 1.7 The exemption for the Landowners stated in 1.6 above has not been provided for Transfer of Development Rights, Long Term Land Lease and Transfer of DRC for construction of a commercial property.

1.8 Under GST law, as per Schedule III, no GST is levied on sale of land. It is submitted that transfer of TDR, Long Term Land Lease and transfer of DRC be treated as akin to sale of (right in) land and hence, no GST should be levied on the same.

1.9 **Recommendation:**

- It should be clarified that any transaction of grant of development rights (via area sharing and/or revenue sharing arrangements) & long term land lease should be viewed as akin to sale of land and hence, should be included in Schedule III of the CGST Act. Accordingly, there should be no GST implications on the same, either on the landowner or the Developer.
- Even for transfer of TDR by way of DRCs, the same should be treated as a benefit arising out of land and thus kept outside the ambit of GST under Schedule III
- If not included under Schedule III, an un-conditional exemption should be given to all types of grant of development rights, long term lease premium arrangements and transfer of TDR by way of DRCs.
- The aforesaid clarification will make a lot of projects viable which otherwise have been stuck due to the increased cost of GST. This will enable Developers to take off many stuck projects resulting in a substantial increase in the absolute GST collection for the Government.

2. **Units handed over to Slum Dwellers / Members of Cooperative Societies / Government Authorities / Land Owners (free of cost) by a Developer under Re-Development / Slum Rehabilitation schemes**

- 2.1 With scarcity of land and a large quantum of old and dangerously dilapidated buildings and large slum pockets in certain metros, Re-development of old buildings or rehabilitation of slums is a highly common development model. Here existing members/residents as part of the redevelopment schemes are allotted units free of cost by the developer in the New Development and the balance inventory is available to the developer for free sale in the open market.
- 2.2 In terms of Notification 3/2019 dated 29.03.2019, GST is applicable @ 5% as if the entire area of the new unit were sold afresh by the Developer to the old Member / Slum Dweller / Government Authorities / Land Owner.
- 2.3 This GST liability works out to be a very huge sum and since the Slum Dwellers and/or Society members do not bear this cost, the developer has to bear the burden of this GST cost which makes such projects unviable. It is as a result of this GST implications that most of the new redevelopment schemes are stuck and the Developers are unable to carry out such projects. As a result the Government is losing huge potential GST revenue which would be earned if such projects take off. It is important to highlight that, a lot of Members are living in old and dangerously dilapidated buildings as a result of a complete dead lock in such redevelopment schemes due to non-viability. The delay caused in the redevelopment of such dilapidated building is resulting in their collapse and grave loss of human life and property.
- 2.4 At this point, it is also important to understand that the value of consideration received from the purchasers of the Developer's free sale units, include the value of cost incurred towards construction done for Slum Dwellers / existing members, which is nothing, but value of constructed area handed over to the Slum Dwellers / existing members. Given this, the units handed over to the Slum Dwellers / existing members under any Rehabilitation and Redevelopment schemes should not be subject to any GST. This is also accepted by Hyderabad CESTAT in case of Vasantha Green Projects vs CCT, GST (Appeal No. ST/31095/2017) and several other decisions.

2.5 Recommendation:

- GST should not be levied on units handed over to the existing members / slum rehabilitation schemes / Government Authorities / Land Owners.

3. GST on sale of commercial units is applicable @ 12% (i.e. 18% less one-third abatement for Land) with ITC credit. Such a high GST Rate has got sale of commercial projects to a complete stand still and further resulting in negligible new commercial developments being taken up by Developers.

- 3.1 When a customer buys a commercial unit today he/she has to pay GST @ 12% plus stamp Duty @ 6% (with minor variation as per the State). This results in an added cost of 18% (12 % + 6%) over and above the value of the commercial unit. This high tax burden is making commercial unit purchases out of budgets of most customers resulting in muted sales for commercial developments.
- 3.2 When GST was made applicable in 2017 there was no distinction between real estate asset classes on the basis of a residential or commercial user and both were taxed initially @ 12% with ITC. After various representations to the concerned authorities there was a clear case to reduce the GST on sale of units to make it more affordable for the buyers. However vide Notification No. 3/2019 dated 29 March 2019, the reduction to GST @ 5% without ITC was surprisingly done only for Residential Developments while sale of Commercial Developments was continued to be taxed @ 12% with ITC.
- 3.3 It is important to note that even in the Service Tax Regime, sale of both residential and commercial units were taxed at the same rate.
- 3.4 Large commercial Developments generally are leased after completion by the Developer and then sold to private equity funds. In such transactions there is no GST applicable as the sale of the project is after completion. However when commercial units are sold under construction to individual buyers GST @ 12% makes it unviable for them to afford.
- 3.5 After COVID-19 there is a growing demand for working closer to home and it makes a great case for incentivising Commercial Developments to grow closer to residential hubs thereby reducing peoples commute time and drastically improving the quality of life of the Indian working population.
- 3.6 With rationalising the GST applicable on Commercial Developments at par with Residential Developments; a large number of Commercial Developments will take off, thereby resulting in a substantial increase in the absolute GST collections to the Government.
- 3.7 **Recommendation:**
Apply the same GST rate for sale of Commercial Units at par with the applicable rates for sale of Residential Units.

4. The current high GST rates applicable on sale of units and on works contracts are substantially curtailing the real estate demand from the end consumer and also making projects unviable for development.

- 4.1 After the roll out of GST, initially the effective tax rate for residential projects (Pre-OC) was provided at 12% with credit (i.e. 18% less one-third abatement for Land) and for affordable housing the effective tax rate was provided at 8% with credit (i.e. 12% less one-third abatement for Land).

- 4.2 The Government vide Notification No. 3/2019 of Central Tax dated 29 March 2019 reduced the rate of tax in respect of residential projects commencing on or after 1st April 2019. The reduced effective tax rate provided are 1% in case of affordable apartments and 5% on construction of apartments other than affordable with restriction on availing Input Tax Credit (“ITC”).
- 4.3 Further, one-time option was provided to the developers for ‘ongoing projects’ to pay tax either at the old rates (effective rate of 8% or 12% with ITC) or on the new concessional rate (1% or 5% without ITC). Accordingly, some developers have opted to continue charging tax at the old rates of 12% or 8% for ongoing projects with ITC while some switched over to the new tax rates.

It is thus evident that post April 2019, multiple rates of GST are in vogue for the Sector with artificial creation of the asset classes. More importantly, the benefit of ITC has been withdrawn for all types of Residential projects and also for the commercial units which are part of RREP. The withdrawal of ITC has not only created the distortions in the ITC chain but has also severely affected the liquidity of the sector. The situation is only going to worsen in the coming days.

It is, thus, essential that the existing tariff structure for the Sector be revisited on priority basis and is harmonized as well as simplified. As the ‘commercial space’ segment is equally bearing the brunt of the impact of COVID-19 and is extremely critical for job creation and sustaining demand for the residential segment, there is a need for extending the benefit of the concessional rate to this segment as well. Last, but not the least, the benefit to ITC is also required to be restored for the Sector as a whole (including redevelopment projects) so as to ensure an uninterrupted, seamless ITC chain. This would not only be in consonance with the basic philosophy underlying GST Policy but would also ease the liquidity problem of the Sector by mitigating the cascading effect of tax.

So far as the “affordable housing” is concerned, if it is felt that the existing rate of GST of 1% (without ITC) cannot be tampered with. Hence it is strongly suggested that a marginally higher GST rate with ITC be prescribed as an option and it may be left to the discretion of the developers engaged in such projects to avail either of the options.

- 4.4 **Recommendations**: In this regard, we would like to humbly provide the possible solutions which should be considered by the Government:

Sr. No.	Category		Existing rate	Recommended rate	Comments
1	Ongoing projects (at old rate)	Residential (Other than Affordable Housing)	12% with credit	8% with credit	Reduced rate would help drive demands
		Affordable housing	8% with credit	3% with credit	

2	New projects (i.e. projects liable to tax at new rate)	Residential (Other than Affordable Housing)	5% without credit	Option to choose from 8% with credit OR 5% without credit	Giving an option may help optimise the GST cost. ITC eligibility will help drive demands.
		Commercial Developments	12% with credit	Option to choose from 8% with credit OR 5% without credit	Rationalising tax on Commercial Developments will incentivise commercial developments thereby creating jobs in residential hubs.
		Affordable housing	1% without credit	Option to choose from 1% without credit OR 3% with credit	
3	Works contract services (for contractors)		18%	12%	The reduction in input services rate would enable the developers to account for the blockage of ITC
4	Works contract services (for contractors providing such services to affordable housing projects)		12%	5%	The reduction in input services rate would enable the developers to account for the blockage of ITC.
5	Services to projects (to cover labour services)		18%	12%	The reduction in input services rate would enable the developers to account for the blockage of ITC.
6	Cement		28%	18%	The reduction in input rate would enable the developers to account for the blockage of ITC.

5. The existing qualification criteria for affordable residential units excludes most of the affordable housing projects thereby not solving the purpose of incentivising affordable housing development.

5.1 Currently the qualification criteria for affordable housing units has a dual threshold of sale value of INR 45 lakhs and carpet area of upto 90 square meters (in non-metropolitan cities/towns) or 60 square meters (in metropolitan cities). The GST rate for the sale of such affordable housing units is prescribed @ 1% without ITC.

5.2 The current project costs (including land cost, approval cost, construction cost and other overheads) for the prescribed carpet area of 90 square meters and 60 square meters in non-metropolitan and metropolitan cities respectively, itself exceeds INR 45 lakhs in many Tier I & II cities across India. Given the high density, the requirement of affordable housing supply is the most in these cities. Due to the aforesaid INR 45 Lakhs criteria, most projects falling within the prescribed carpet area limit do not qualify as affordable housing units under the existing definition of 'Affordable Housing Units' in the GST regime, thereby denying the intended benefit of the policy to the deserving sections of our society.

5.3 **Recommendation:** Following definition of "Affordable Housing Unit" may be adopted:

- "Affordable housing unit means a unit with carpet area as defined under RERA that does not exceed 60 square meters in the metros and 90 square meters elsewhere."

6. **Eligibility of input tax credit of the cost of construction incurred for development of a commercial property is not available for set off against the GST charged on the rent/lease received from renting/leasing such commercial premises.**

6.1 In many instances the Developer / Land owner constructs a commercial building with the sole purpose of renting out such premises to lessees or tenants such as business houses, service providers, retailers, restaurants, hoteliers, theatres, hospitals, etc. all of which generate employment and contribute to the growth of the economy and GDP.

6.2 As per the current GST law, any lease or letting out of such constructed immovable property is deemed to be a service and taxable under GST at the proposed rate of 18%. However, as per Section 17(5) of GST law, it appears that input tax credit of the cost of construction incurred for development of a commercial property or any repairs carried out is not available for set off against the GST charged on the rent/lease income received from renting/leasing such commercial premises.

6.3 There is ongoing ambiguity on whether the aforesaid input tax credit under GST is allowed or not for goods and services used for construction of immovable property (except plant and machinery) where such property is not further sold but leased out or used as hotel/ resort etc. Many developers are not claiming such credit leading to increase in tax cost for the renting company.

6.4 We would like to highlight that the output of renting/ leasing attracts GST at 18% - however, if the input tax credit for construction (including renovation, repair, alteration etc) is disallowed, it would be against the principle of GST to provide a seamless credit chain. The foundation of GST regime was to allow credit offset across the entire transaction chain and such credit restriction leads to a blockage of credit and hence, increases tax costs.

6.5 In this regard, reference is made to the recent decision of the Odisha High Court in the case of Safari **Retreats Private Limited Vs. Commissioner of Central Tax (CGST) & Ors** [2019-TIOL-1088-HC-ORISSA-GST] wherein it was held that input credit on purchase of goods and services for construction of a mall (by the applicant) should be eligible to be availed and utilised against output services by way of commercial renting of the mall and the credit restriction should not apply in such case. The following key aspects were held by the Hon'ble High Court:

- Purpose of GST is to make uniform provisions for levy and collection of tax, intra state supply of goods and services both central and state and to prevent multiple taxation.

- The narrow interpretation of Section 17(5)(d) of the GST Act to disallow credit is frustrating the very objective of GST Act and hence, the same should be read down and the narrow restriction as imposed is not required to be accepted
- It was held that if the assessee is required to pay GST on rental income arising out of investment on which he has paid GST, it is required to have input credit on the GST

The matter is pending before Hon'ble Supreme Court of India. Several other writ petitions have been filed and admitted in High Courts across the country challenging the ITC restriction in such cases.

- 6.6 We further wish to submit that the ITC restriction leads to enhanced cost burden on the total cost of construction of the property and will escalate the project costs. Moreover, high rate of GST on inputs/input services will have an adverse impact on the working capital of the company especially at the prevailing situation of decelerating growth and COVID-19.
- 6.7 It is also submitted that globally, such input tax credit is allowed to all developers as the output service also attracts GST/ VAT (as applicable in such countries).
- 6.8 **Recommendation** - It is suggested that the restriction to avail the aforesaid ITC should be removed to ensure seamless flow of credit to businesses where the property being constructed is being used for further providing an output service (such as renting, hotels, malls etc).

7. Time Limit for issuance of credit notes for cancellation

- 7.1 CREDAI is positive that the real estate sector would overcome the COVID-19 hurricane. However, it is also an accepted fact that the sector may have to face cancellation of bookings in the immediate future.
- 7.2 As per existing law, credit note for cancellation of booking and adjustment of GST paid on same is allowed only till end of September of the next financial year
- 7.3 In the real estate industry construction activity takes place over a span of 2 to 5 years. Due to this typical nature of the industry cancellations can take place anytime during this period. GST paid at the time of booking and further milestones should be allowed to be reversed by issuance of credit note at the time of cancellation of booking. Keeping a time limit for reversal of such GST paid impacts the Developer and customer both.
- 7.4 **Recommendations:**
- Issuance of credit note and reversal of GST paid should be allowed without any limit upto the month of receipt of completion certificate or first occupation, whichever is earlier.
 - Section 34 of CGST Act should be amended to allow issue of credit note on cancellation of flat or commercial premises to enable the Developer to adjust the tax refunded on cancellation against tax payable for the month in which such cancellation happens or in subsequent months.

CREDAI sincerely believes that the above immediate relief measures would enable the beleaguered and badly bruised Real Estate Sector to tide over the present crisis, remain afloat and ensure its sustenance, stability and ultimate revival. The suggested relief measures would also serve as a strong basis for the much-needed comprehensive overhauling of the GST structure for the Sector in future.

CREDAI strongly believes that in the long run, if not in near future, a comprehensive coverage of the entire Sector including the transaction in 'land and buildings' within the scope of GST and consequential subsuming of all the State level and/or Municipal levies including stamp duty is inevitable which will only pave the way for the robust growth of this crucial Sector and also in achieving the dream of Hon'ble PM of 'Housing For All by 2025'.

CREDAI sincerely hopes that the suggestions for the immediate relief measures outlined above will be considered positively and the suggested measures will be announced expeditiously. We shall be grateful if an opportunity is provided to discuss the suggested measures via Video Conferencing or in person, on a suitable date and time, as may be advised.

We request you to take the above submissions into consideration in the upcoming GST council meeting and provide the much needed relief to the real estate sector.

Thanking you,

Yours Faithfully,
For CREDAI-MCHI



Deepak Goradia
President



Pritam Chivukula
Hon. Secretary