

Ref. No. MCHI/PRES/17-18/082

December 18, 2017

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To,
Shri Dinesh K. Jain (I.A.S.)
Additional Chief Secretary (Finance)
Finance Department
5th Floor, Main Bldg., Mantralaya
Mumbai - 400032

19/12/17
अवर मुख्यालय (वित्त)
यांचे स्वामि सहायक
वित्त विभाग, मंत्रालय,
मुंबई-४०००३२.

Sub: Representations and suggestions with regard to certain changes required in levy of GST on the transactions pertaining to the real estate sector, so as to avoid inflationary impact on real estate prices.

Respected Sir,

1. At the very onset, please accept our heartfelt gratitude to have kindly accepted to and grace our MahaProperty Expo on the 17th November, which was a historic moment for the entire Real Estate Industry in MMR.
2. In your opening remarks, you had mentioned that it was absolutely safe to buy a house at the Maha Property Expo organized by CREDAI - MCHI as all the projects were Maha RERA registered & approved. You had also mentioned that EODB and Maha RERA have been a success not because the Government had done it but because of the joint (developer fraternity) participation in the entire process.
3. Sir, while commenting that Demonetisation, RERA and GST have been the real estate industries endurance test, you had unequivocally acknowledged the fact that you were aware that still lots of problems need troubleshooting. Sir, as expected by, we ensure that we shall always work together with your government in all your initiatives and work towards making the maximum contribution to the GDP in the future.
4. As one of the areas that requires immediate troubleshooting, we would like to draw your kind attention to certain matters pertaining to the levy of GST in the real estate sector, which have the domino or cumulative effect of increasing the prices of constructed premises, including houses, due to the incidence of the levy of GST in its existing form. Such increase in the incidence of indirect taxes like GST is bound to ultimately lead to an increase in the cost of constructed premises and consequently housing.
5. In the earlier regime, cost of service tax after abatement was 3.75% or 4.50% and after the adjustment/ set off of input tax credit the actual implication or tax incidence was approximately 3% to 3.5%. The cost of VAT under composition scheme was 1% with no input tax credit against the same. Thus, the actual net incidence of indirect taxes was only 4% to 4.5%. The tax rate under GST regime is stipulated at 18% in case of sale of under construction flats and after allowing presumptive deduction for land cost at 1/3rd of sale value of the flat (that too only in some cases), the effective tax rate comes to

12% of the price of the flat. In certain other cases, considering the possible interpretation of the current provisions of the applicable GST legislation the implication could even be 18%. The set off available against GST liability of 12% or 18% is barely 2.5 to 4% (approximately) for sale of under construction flats in urban area since there would be no GST on a large component of the costs (like land costs and approval costs) to be incurred by the real estate developers. In addition, thereto, for the reasons explained in the annexures to this letter, we have proposed that your good self be pleased **to consider our proposal of levying a presumptive GST at a flat rate of 4% to 5% on sale price of under construction project without granting any input tax credit (with simultaneous non-taxability of development rights, TDR, lease hold premium etc.) or alternatively allow deduction of land cost at reckoner value on the date of sale of flats.** Either of these proposals would result in tax incidence for the consumer almost equivalent to the pre-GST regime tax incidence on purchase of under construction premises. Under the said proposals, there is a minimal or no effective loss of revenue for the exchequer as compared to the existing provisions of levy of GST.

6. For ease of explaining hardship under various provisions of GST to the real estate sector, we have annexed hereto a comprehensive note of various provisions under GST and the consequent concerns and issues arising therefrom as well as certain suggestions thereon for your kind consideration.
7. We humbly request your goodself to kindly consider the issues and suggestions enclosed herewith in a favourable light and after such consideration to kindly make necessary and suitable amendments in terms of the enclosed suggestions so that the implementation of GST does not result in increase in cost of housing for the citizens of the country.
8. We would be happy to respond to any queries that you may have or clarifications that you may require with regard to the subject matter hereof.

Our humble request:

1. **Kindly levy a presumptive tax at 4% to 5% on sale price of under construction project without any input tax credit or alternatively, reduce the tax rate and increase the land cost deduction to lower the increased burden of Tax under GST regime.**
2. Kindly exclude Development Rights, TDR, Tenancy Rights and Leasehold Rights in immoveable properties from purview of the GST these being rights in immoveable properties arising from Land and Building.
3. Kindly allow land cost deduction in cases of projects where the consideration is inclusive of price for land rights where the land rights are given by the Society or the JV partner or any Government Agency, freehold or leasehold.
4. Kindly allow exemption from applicability of tax under GST in respect of grant of long term leasehold rights in land being in the nature of conveyance.

5. Kindly allow exemption from applicability of tax under GST in respect of affordable housing for urban poverty alleviation, slum rehabilitation, cluster developments and old tenanted buildings and cooperative societies.
6. A meeting be granted to our office bearers to explain need and justification of the above requested amendment to give real boost to Affordable Housing.

Thanking you

Yours faithfully,
For CREDAI-MCHI



Mayur Shah
President



Domnic Romell
Hon. Secretary



S. S. Hussain, I.A.S. (Retd.)
Chief Executive Officer

Annexure to our letter of representation on GST

1. Steep hike in tax rate on sale of under construction flats:

Relevant provision:

The tax rate is stipulated at 18% in case of sale of under construction flats vide notification no 11/2017- Central Tax (Rate) dated 28.06.2017.

After allowing presumptive deduction for land cost at 1/3rd of sale value of the flat, the effective tax rate comes to 12% of flat value.

Concerns and issues:

- a. A presumptive deduction of 1/3rd of sale value of flat has no correlation to the actual cost of the land in a project. The 6% deduction in most cases is not nearly commensurate to the cost of land vis-à-vis the cost of construction. The actual cost of land differs from area to area, city to city. Moreover, in metros, cost of land is major component of the cost of a project and it almost always exceeds 33%. **This indirectly results into levy of GST on land value which is not in consonance with GST legislation which specifically excludes land from scope of supply and/or levy of GST.**
- b. The aforesaid can be easily understood with the help of following example:

		Premium Location	Medium Location	Remote Location
		Rs per sq feet		
Sale price	A	70,000	40,000	5,000
Land cost	B	50,000	27,500	1,000
Presumptive Deduction for land cost (1/3 rd of A)	C	23,333	13,333	1,667
Value of land on which GST is paid (B - C)	D	26,667	14,167	-
Tax @ 18% on short deduction against land cost (D x 18%)	E	4,800	2,550	-
Excess tax on sale price (E / A)	F	6.86%	6.38%	

- c. Such a presumptive deduction of 1/3rd of the sale value of the flat (being attributed to the cost of land) is illogical in as much the ratio of land cost to construction cost can never be fixed in all cases regardless of the location of the land. The construction cost in various locations may not be differential but there would definitely be a huge price/market value difference in the land cost, therefore, the 1/3 : 2/3 ratio between land cost and construction cost cannot be fixed across the board for example in a metro city like Mumbai, the cost of land (on a per square feet basis) is much more than the cost of construction (on a per square feet basis) and in fact in some cases the land cost is more than 10 times that of the construction cost. Such standardised ratio being applied across the board for the deduction in land cost is therefore not only unfeasible but also impractical.

- d. In GST regime, the transaction cost for acquiring a house under construction for the citizen will rise substantially and become unaffordable as illustrated below:

	Pre-GST	Post-GST (with land cost deduction)	Post-GST (without land cost deduction)
Stamp Duty	5.00%	5.00%	5.00%
VAT	1.00%	-	-
Service Tax	4.50%	-	-
GST	-	12.00%	18.00%
Total Tax Cost	10.50%	17.00%	23.00%

- e. Incidental cost of Stamp Duty and GST being 17% / 23% of value of a flat will be unbearable burden for a citizen buying a house in metro cities especially when they put their life time savings in buying a house, in addition to taking a new home loan. This will consequently result into slowing down the demand in already sluggish real estate market in most of the Metros and other Cities. The above cost of Stamp Duty and GST is in addition to the approvals costs (payable to municipal corporations) are very high adding to the cost of flat.
- f. Most importantly, all costs that are incurred by the real estate sector do not suffer GST like, land cost, approval cost, finance cost and employees cost do not suffer GST. The Government is under a bona-fide belief that real estate developers will be eligible for input tax credit of material and passing that credit to customers will offset the rise in the tax rate. In reality, impact of additional input tax credit available on materials and contracts in GST regime is very nominal as compared to hike in effective tax rate particularly in cases where the actual land cost is in multiples of the construction cost. The cost of construction (material and services) is usually in the range of Rs.4,500/- per square feet. Average input tax on such construction cost comes in the range of Rs.900/- per square feet. Assuming that the selling rate of flat is Rs.40,000/- per square feet, additional output tax is 6.50% of Rs.40,000/- i.e. Rs.2,600/-. The net tax incidence on customer would Rs. 1,700/- per square feet even when developer passes on input tax credit of Rs.900/- to customer. The additional tax incidence is 4.25% of flat value which is exorbitant from any standard.
- g. This incidence (with minimal set off against the input depending on the location of the property) would ultimately be passed on the actual consumers and is thus bound to increase the cost of housing; and the same will not be socio-economically desirable.

Representation and suggestion:

- i. It is suggested to levy a presumptive tax at 4% to 5% on sale price without any input tax credit coupled with non-taxability of development rights, TDR, leasehold premium and any such rights in immovable property. This matches with pre-GST regime tax incidence on purchase of under construction flats. In fact such a reduced presumptive tax at 4% or 5% without any corresponding input credit will not even have any substantial adverse impact on the aggregate quantum of the GST collected by the Government and will not result in any substantial revenue loss to the exchequer.

For example, transactions in respect of jewelry are presently taxed at a flat rate of 3%. Like jewelry, buying a developed real estate property is an extremely high value transaction; and it is a permanent investment for the buyer. An average citizen does not acquire housing on a regular basis. In view of this, a flat levy of GST at 4% to 5% rate without any set-off or input tax credit, would be justifiable for sale of under construction premises.

The usual net profit margin of real estate developer is nearly 15% to 20% and tax at 18% thereof comes to around 2.70% to 3.60%. This also justifies the lower suggested rate of 4% to 5% on sale of flat.

Moreover, though the anti-profiteering policy of the Government is suggestive of the principle that the input tax credit is to be passed on to the ultimate consumer, the exact quantum of the same will not be verifiable by the consumer at the time of purchase of flat or even known to the real estate developer at the time of sale of the flat. The price of the sale of the constructed premises will have to be finalised and closed (in the interest of certainty) at the time of execution of the agreement itself. However, on the contrary, if the flat rate method of levy of GST (without any corresponding benefit or deduction of input tax credit), as suggested hereinabove, is adopted by the Government, then the exact quantum of applicable GST will be known to the consumer and the transactions would become extremely transparent.

- ii. In the alternative to the aforesaid suggestion, we suggest that the applicable tax rate of GST be reduced generally to 12% , whilst allowing deduction of input tax credit and the same also allow for deduction/credit for actual cost or market value (whichever is higher) of the land for working out the actual taxable value of construction services.
2. **Clarity on availability of deduction of 1/3rd in respect of sale of under construction flats on leasehold land or where construction is done on land pursuant to acquisition of development rights:**

Relevant provision:

Paragraph 2 of Notification 11/2017-Central tax (Rate) dated 28/06/2017:

“in case of supply of construction service **involving transfer of property in land or undivided share of land**, as the case may be, the value of supply of service and goods portion in such supply shall be equivalent to the **total amount charged for such supply less the value of land or undivided share of land**, as the case may be, and the value of land or undivided share of land, as the case may be, in such supply shall be deemed to be one third of the total amount charged for such supply.

Concerns and issues:

The notification stipulates presumptive deduction of 33.33% in respect of transfer of land or undivided share in land.

However, it is not clear if the word “transfer” includes leasehold transfer or a transfer contemplated in the future (on completion of construction) in favour of body of members like a co-operative society, association of purchasers, etc.

In cases where construction is done on leasehold land or where construction is done on land pursuant to acquisition of development right, the lack of clarity on the above referred aspect could lead to a possibility of denial of presumptive deduction. This could result into tax demand of 18% instead of 12%. In order to cover themselves

against such probability of a demand @ 18%, real estate developers are likely to charge GST @ 18% to the purchasers or include such tax incidence in the purchase price, thus ultimately elevating/escalating the housing costs.

In all cases of sale of constructed premises, where the Real Estate (Regulation and Development) Act, 2016 ("RERA") is applicable, the Promoter is ultimately required to convey title in the land (which may be freehold or leasehold) to the unit purchasers or a body of unit purchasers like a co-operative society or association or other legal entity. Thus such a provision of permitting a conditional set off of 6% has no applicability in cases where the provisions of RERA are applicable as there is a statutory requirement of transfer of title of the Promoter (either freehold or leasehold) in land. Each purchasers of a unit may not actually hold "undivided share" in the land but the entire land may be conveyed to a legal entity, wherein all unit purchasers are members/shareholders. Therefore, the qualification of a transfer of "*undivided share*" in land is misplaced and the issue should be suitably clarified.

Representation and suggestion:

The notification should be further suitably clarified to provide for presumptive deduction even in cases where construction is done on leasehold land or where construction is done on land pursuant to acquisition of development right with an ultimate provision of a conveyance of freehold title or leasehold title in favour of the purchasers or body of purchasers.

3. Tax implications on purchase of development rights, transferrable development rights (TDR), floor space index (FSI) and tenancy rights:

Relevant provision:

Section 9 of CGST Act stipulates GST levy on supply of **Goods and/or Services**.

Section 2(52) of CGST Act defines 'goods' to mean every kind of **movable property** other than money and securities. Thus, immovable property is not 'goods' and cannot under circumstances be qualified as such.

'Service' is defined u/s 2(102) of CGST Act to mean 'anything other than goods, money and securities'.

Immovable property, not being goods, will be a 'service' as defined u/s 2(102) of CGST Act. However, it is not feasible that a transaction of transfer of immovable property or rights therein (without there being any value addition be made subject to GST).

Clause 5 of Schedule III to CGST Act excludes only the following from scope of supply:

- Sale of land
- Sale of building (other than under construction sale of flats/unit)

Concerns and issues:

Schedule III excludes "sale" of land and building from the scope of supply.

The development rights, TDR, FSI or even grant or transfer of tenancy rights or long term leases are rights arising out of land / building but it may not be regarded to be land / building and are considered as immovable property per se. However, the same are treated as "immovable property" since it is settled law that anything emanating from land or permanently fastened to land or permanently attached to

land. Various counts including the Hon'ble Bombay High Court and the Hon'ble Supreme Court of India in a plethora of judgments have held that the development rights and TDR are "*immovable property*".

An apprehension, therefore, is that acquisition of development rights, TDR, FSI, tenancy rights, etc is liable to GST and it will be taxed at 18%.

Levy of CGST on such rights under GST tantamount to taxing land which is not in consonance with GST legislation and also the constitution.

Further, such liability needs to be discharged upfront on execution of agreement in addition to payment of stamp duty of 5% on development rights agreement without actual realization and/or accruals or benefits to the concerned transacting parties. This entails cash outflow of 23% (18% GST + 5% Stamp Duty) upfront adversely impacting real estate developers, particularly in Mumbai, where practically all projects are done by acquiring development rights, TDR, tenancy rights, etc.

Under General Clauses Act, the term 'immovable property' is defined to include any benefits arising out of land. The development rights, FSI, TDR, etc are 'immovable property' under general law.

Section 65B (44) of the Finance Act, 1994 excluded transfer of '*immovable property*' from scope of 'service'; and hence transfer of above referred rights were not liable to service tax.

We are sure that it cannot be the intention of the Government to levy GST on such transactions, which in essence are nothing but 'transfers' of immovable property. However, due the language used in the existing legislation, the position today is quite obfuscating and it is of extreme importance that this position be clarified. The language presently used, could have an interpretation or it could be implied therefrom that GST could be levied on such transactions, which are actually in the nature of a simpliciter sale or other mode of transfer of immovable properties which do not technically qualify as a "sale of land" or "sale of building" but in essence are transactions of transfer of immovable property without there being any value addition to such immovable property or actual provision of any service.

It may also be mentioned at this juncture that the levy of such a tax on transactions of sale/transfer of immovable property and falls within the purview of a State Government and not the Central Government under the Constitution of India and such a levy may thus be amenable to challenge on such ground.

Further, State Government already levies stamp duty on transfer of such rights and hence levy of SGST on the same will lead to double taxation.

Representation and suggestion:

The scope of supply should be amended to exclude all types of transfers in respect of all rights arising out of immovable property such as development right, TDR, FSI, tenancy rights, etc.

Tax implications in respect of purchase of leasehold rights:**Relevant provision:**

Clause 2(a) of Schedule II to CGST Act, **deems lease as supply of service.**

Concerns and issues:

In cases of a long term lease there are usually two components of payment by the lessee to the lessor. One is a premium which is generally paid as a one-time consideration and a recurring lease rent. The existing provisions do not acknowledge this distinction and therefore it may be possible that there would be an implication of GST on the amount of premium paid on a long term lease. Such premium is actually in the form of consideration for transfer of immovable property and the same should be specifically excluded from the applicability of GST.

Premium or salami paid for long term lease of 30 years, 99 years or 999 years (perpetual lease) will also be covered under supply of service liable to GST at 18%.

Long term leases are almost at par freehold transfer of land. Levy of CGST on premium for such leases would tantamount to taxing land which is not in consonance with the principles of levy of GST and also the Constitution of India, as the same will amount to a tax on a transaction of transfer of immoveable property. State Government already levies stamp duty on such transaction and hence levy of SGST thereon amounts to double taxation on same transaction.

GST liability on leasehold premium amount will be payable upfront on payment of lease premium in addition to payment of stamp duty of 5% on such lease deed. This entails or approximate cash outflow of 23% upfront adversely impacting real estate developers in Mumbai, Navi Mumbai, Panvel, etc where construction is done on leasehold plots.

Entry 41 of Notification No. 12/2017-Central Tax (rate) dated 28/06/2017 provides exemption to one-time upfront amount paid to State Government industrial development corporation for **grant of long term lease of 30 years or more in respect of industrial plots. No such exemption is granted for residential plots.**

Representation and suggestion:

Exemption on the line of industrial plot is granted for leasehold premium paid on residential plots also.

4. Adjustment of tax on cancellation of flats:**Relevant provision:**

Section 34 of CGST Act provides for such adjustment in following cases only:

- Taxable value or tax charged thereon exceeds actual taxable value or tax payable.
- Sales return
- Deficiency of service

Concerns and issues:

Rule 6(3) of Service tax Rules, 1994 permits a real estate developer to adjust service tax refunded on cancellation of flats/ units (non-provision of service) to customer against tax liability of the month in which such cancellation is done.

However, section 34 of CGST Act does not permit adjustment of GST refunded against tax liability in case of cancellation of flat booking (Non provision of service). The applicable provisions should be amended to permit such adjustment of GST in case of cancellation of transaction for purchase of constructed flats/premises, since the applicable GST would be paid on the subsequent sale/transfer of the same flat/premises.

Section 54(8)(c) of CGST Act permits refund of tax paid on supply which is not provided either wholly or partially. This refund is permitted in the case where invoice are not issued. The builders are obliged to issue the invoice on receipt of installments due. Builders will therefore, may not be in a position to apply for refund under this section. Moreover, limitation period of 2 years is prescribed for refund, Builders will not be in a position to go for refund.

Representations and suggestions:

Section 34 of CGST Act be amended to allow to issue credit note on cancellation of flat to enable builders to adjust the tax refunded on cancellation against tax payable for the month in which such cancellation happens or in subsequent months.

5. Reversal of ITC on non-payment of consideration to vendors within 180 days:

Relevant provision:

2nd Proviso to Section 16(2) of CGST Act provides that where recipient fails to pay the supplier (or service provider) the value of supply along with tax payable thereon within 180 days from the date of issue of invoice an amount equal to ITC shall be added to output tax liability along with interest thereon.

Concerns and issues:

- i. In GST regime, vendor is obliged to pay GST on accrual basis and he discharges GST liability irrespective of realisation of consideration. As the Government has already realised tax on accrual basis, there is no justification in holding back the tax credit of the person acquiring such supplies on delay of stipulated period in payment to vendors. The credit period and delay in payment to the vendors are business exigencies and there is no justification for the Government to intervene in this area.

Further, such provisions unnecessarily complicate the record keeping of the supplier/service provider and also poses challenge for tax authorities to monitor such provisions.

- ii. Joint development and re-development projects involve barter of development rights and construction services. It appears that supply of development rights is taxable and developer is entitled to ITC in respect of such development rights. Developer usually discharges consideration for development right by handing over constructed flats to land owner / society on completion of project and developer will be entitled

to ITC on such date. Developer will be unable to utilize such credit as he may not have any output tax liability post completion of project. Refund of accumulated ITC balance is not permissible for real estate sector and hence such ITC will be a dead loss for developers.

Representations and suggestions:

2nd proviso to Section 16(2) of CGST Act should be deleted.

6. Availability of input tax credit to the real estate developers:

Relevant provision:

Section 17(5)(c) of CGST Act provides that input tax credit shall not be available in respect of works contract services when supplied for construction of an immovable property **except where it is an input service for further supply of works contract service.**

Section 17(5)(d) provides that input tax credit shall not be available in respect of the goods or services received by a taxable person for construction of an immovable property **on his own account.**

Concerns and Issues:

There is an apprehension that a view could be taken by the authorities that a real estate developer provides construction services and not works contract services and hence the real estate developer is not entitled to ITC credit on works contract service he avails for construction of building for sale. Similarly, another apprehension is that if such a view is taken by the authorities that real estate developer is constructing building on his own account, the applicable ITC in respect of goods and services used for construction might be jeopardized under Section 17(5)(d) of the CGST Act. These provisions require to be clarified to leave no scope for ambiguity.

Representation and Suggestions:

Section 17(5)(c) and 17(5)(d) should be amended and clarified to provide expressly that real estate developers selling under construction premises are entitled to input tax credit in respect of all goods and services procured by such developer for construction of premises for sale.