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Ref. No. MCHI/PRES/19-20/041

September 16, 2019

To

Shri Rajiv Jalota (I.A.S)

Commissioner

State Tax, Maharashtra State

GST Bhavan, Mazgaon,

Mumbai - 400 010.

क.स.स. महाराष्ट्र,
राज्यकर आयुक्त,
वस्तु व सेवा कर विभाग,
महाराष्ट्र राज्य भुवई,
ग्रामे कार्यालय.

Subject: Issues and suggestions relating to GST on Construction services in the Real estate sector

Respected Sir,

We express our sincere thanks and appreciate the efforts by Government of India under your leadership to boost the economy as a whole as per the recently announced financial/economic reforms.

CREDAI-MCHI is an apex body consisting of members from the Real Estate Industry among representing 1400 developers spread Mumbai Metropolitan Region (MMR). CREDAI-MCHI has been pursuing a policy framework in which the best of private sector talent and resources are directed towards achieving Housing for All by 2022 through employing technologies appropriate for 21st century urban India. CREDAI-MCHI integrates advocacy for housing and habitat with activism on consumer protection, labour welfare, skill development and sustainability.

As you are aware that after agriculture, we are 2nd highest employment generating sector in India. We at CREDAI-MCHI are aligned to the vision of our Hon'ble Prime Minister of "Housing for All" by 2022. On this path of shelter and employment creation, we have received continuous support from the Government in the past 5-6 years. With the recent impact of global economy in general, we are also facing few sustainability challenges. One such challenge is making real estate affordable for all. While doing so, we need your urgent attention and support in solving certain past and present issues under GST. The issues highlighted in the below submission are genuine and if not sorted out would have an adverse impact on majority of real estate developers across India catering to the needs and requirements of middle and working class of India.

Before making any specific suggestion, we would like to re-iterate our submission that the real estate sector needs a rational GST rate with input tax credit being allowed. We have seen that the new GST rates without input credit are resulting into increase in cost and ultimately increase in prices of the under-construction units. We request your good self to re-think on the core principle of GST which was "seamless flow of credit" and allow the sector to avail input credit for all types of construction activity. GST rate on construction services should be rationalized to see to it that the developer and customer both are in a win-win situation.

Since some of the issues are relating to past period of July 2017 to March 2019, if sorted they will also support your humble intention of reducing litigation.

1. GST on Development Rights

As you are aware that the real estate sector works on multiple models, one of which

is by way of transfer of development rights to the developer for executing construction activity. Under this model the landowner parts away with his land for a consideration to be received in monetary or non-monetary form.

In most of these cases, the landowner at some stage of the construction activity (start, middle or end), gives away his ownership in the land component. Given this, it can be termed as an indirect sale of land. Even the stamp duty acts across India, consider it as a transaction equivalent to sale of land.

Service tax to some extent and now GST, tries to give it a flavor of service transaction attracting tax. In other words, land component is being subjected to GST by treating it as service of transfer of development rights. This is against the basic principles of the Constitution of India that GST cannot be charged on land component.

Assuming for the time being that the credit being eligible on payment of tax on such development rights, still there is a blockage of capital, that too merely on account of the allotment of area to the landowner which does not provide any cash inflows to make payment of such liabilities.

Further, in a typical built up area sharing, the allotment is made on the date of completion since the landowners intend to own such property for investment or own residence. The payment of GST by the landowner on the date of completion makes the Input Tax Credit (ITC) as ineligible since there is no output liability to be adjusted against the same. The law doesn't even permit refund of such ITC to the developers under the refund mechanism. Such investment in the overall project considering the ITC on development being no more an eligible credit makes the developers to consider it as cost and mark up in the sales price making the overall unit cost to go up and no more as affordable.

After making multiple submissions, the Ministry has provided some relief to the developers constructing residential units from the development rights received on or after 1st April 2019. Now due to revised GST scheme for real estate sector that became effective from 1st April 2019, we have been given a partial exemption on such type of transactions.

We need your urgent attention to provide us with a one-time exemption for all such cases upto 31st March 2019. This will help us to free up some portion of the real estate inventory which is blocked due to increase in cost on account of GST applicability on land component of the sale.

This will help lot of developers in all parts of India to sell off constructed inventory at a reasonable sale price and release themselves from the burden of interest.

Since the matter is contentious, it is likely to be in the court of law sooner or later. Providing a one-time relief to past cases aligned with an already implemented scheme for new projects effective 1st April 2019, the chances of litigation on the subject would be negligible.

If the above submission is acceptable to the your good self, we also request you to re-think on the basic premise of charging GST on land component and giving an unconditional exemption to the following types of rights even for future cases:

- a. Assignment of right to purchase immovable property;
- b. Supply of additional FSI/ transferable development rights;

- c. Development rights under Joint Development Agreements;
- d. Transfer of TDR Scrip (generated out of compulsory/ optional acquisition of land)

Why are we seeking this benefit?

The moot reason is, in an economy where cash flows today play the most important role, the above model used by the developers, is one of the most sought after option wherein the cash outflow for land procurement is very minimum (in most cases nil). This helps in faster completion of the projects since the funds are used directly towards construction activity and not towards land procurement. If the above relaxation (which is aligned to the framework of the Constitution of India) is given, more and more projects will be executed on this model and it will result into reaching the target set under "Housing for All" at a faster pace.

2. GST on Long Lease Premium

As you are aware that land parcel in many parts of India are also provided on long lease basis. Based on the tender process, the land parcel is allotted to the bidder for development. Generally, Landowner allows the bidder a period of 45-75 days to make the full payment of long lease premium. Landowner in certain cases can also extend the period of payment subject to interest for the delay. Once the full payment is received, the land parcel is handed over by entering into a Long Lease Agreement for a period of more than 30 years (generally).

Landowner(s) have been collecting GST on the Earnest Money Deposit (EMD) and the lease premium at 18%. This GST collected and paid to the Government kitty was available to the Developer as input tax credit till 31st March 2019 (under the erstwhile GST scheme as applicable to the Developers).

Various Developers and Associations have made representations to the GST Council that GST on Long Lease premium should be exempted as the same is nothing but an indirect arrangement for sale of land. Taking this into consideration, the GST Council had brought in amendments in the GST scheme applicable to Developers in March 2019. One-time option to continue with old scheme (charge GST at old rates and take input credit) was allowed to ongoing projects by the revised GST scheme which was effective from 1st April 2019.

As explained above, the ongoing projects were allowed an option to continue with the old scheme. However, for a project to qualify as ongoing project, it had to fulfil the following conditions as of 31st March 2019:

- a) Commencement certificate for the project has been issued by competent authority (if required)
- b) Construction for the project has started on or before 31st March 2019 and the same is certified by Architect or chartered engineer or licensed surveyor
- c) Completion certificate has not been issued or first occupation for the project has not taken place
- d) Apartments being constructed under the project have been booked partly or wholly

Many Developers across India opted for this scheme. However, there are many cases wherein the Developer has paid EMD and/ or few instalments of long lease premium. In such cases the lease agreement was yet to be entered as on 31st March 2019 and the period of lease going to start on or after 1st April 2019. The Developer

in such cases could not apply for commencement without a lease agreement. Due to revised GST scheme, wherein these kind of cases do not qualify as ongoing project, the Developer has no other choice but to pay GST at 5%/1% and forgo input tax credit. The quantum of GST paid to Landowner for all such cases have now become a cost to the Developers. If for the sake of quantification, we assume that 30% of the allotments made by CIDCO (in Navi Mumbai, Maharashtra) during 2017 to 2019 fit into this case, we have a GST amount of INR 46.64 Crore which is now not available as input credit to the Developers doing projects only in Navi Mumbai city of Maharashtra. This would be the case across many cities in India wherein infrastructural development is based on long lease basis.

The per square feet cost is likely to increase by approximately INR 750. This is going to hit the prospective customers adversely.

As highlighted above, the whole issue of non-eligibility of input credit that too the one which is charged on a transaction which should have been exempted (indirect sale on land) is not going to support the Government's mission of "Housing for all".

To deal with this situation, we suggest the following measures could be adopted:

- Option 1 - All projects where GST was paid on land component but was not allowed as input credit (due to reasons listed above) be allowed an option to still opt for old scheme (and continue to enjoy benefit of input credit)
- Option 2 - Government should allow a one-time refund scheme for all such projects wherein the GST component was paid on land and the same was not allowed as input credit

Either of the above, would provide a breather to such projects and help them be at par with the other projects which qualified as ongoing and took input credit of the GST paid on long lease premium.

3. GST Rate of 8% with ITC to be Restored

The real estate sector needs a rational GST rate with input tax credit being allowed. We have seen that the new GST rates without input credit are resulting into increase in cost and ultimately increase in prices of the under-construction units. We request your good self to re-think on the core principle of GST which was "seamless flow of credit" and allow the sector to avail input credit for all types of construction activity. As granting seamless input tax credit is the basic crux of indirect taxation laws, we do hereby humbly request the government to give the developers an option to pay GST @8% with input tax credit.

4. GST on Development Rights Used for Commercial Construction

As you are aware, GST is applicable on construction services provided by the builder/ developer. When a developer provides these services, the nature of the activity does not change whether it results into creation of residential or commercial units.

GST law till 31st March 2019 was also aligned giving similar treatment to both types of construction. However, with effect from 1st April 2019 under the revised GST scheme for real estate sector, commercial construction was not given the treatment at par with residential construction. Commercial units are subject to GST at 12%/5% as compared to residential units which are subject to 5%/1%. Similarly, the

exemption from GST on development rights is also not given to commercial units. Also, the developer is required to maintain all details for availment of credits in cases where the commercial portion of the project crosses a particular limit.

Along with Housing for All, the current government also focuses on skill development, entrepreneurship development, self-employment generation opportunities, assistance in setting up businesses by way of Mudra loans etc. Commercial units i.e. shops, offices, godowns, etc. play a vital role in fulfilling this aspiration of budding businesses.

Assuming for the time being, that the credit being eligible on payment of tax on such development rights, still there is a blockage of capital, that too merely on account of the allotment of area to the landowner which does not provide any cash inflows to make payment of such liabilities.

Further, in a typical built up area sharing, the allotment is made on the date of completion since the landowners intend to own such property for investment or rental use. The payment of GST by the landowner on the date of completion makes the Input Tax Credit (ITC) as ineligible since there is no output liability to be adjusted against the same. The law doesn't even permit refund of such ITC to the developers under the refund mechanism. Such investment in the overall project considering the ITC on development being no more an eligible credit makes the developers to consider it as cost and mark up in the sales price making the overall unit cost to go up and no more as affordable.

Construction of commercial units in and around residential project is a typical sale model for the developers since the residential units shall require commercial units to provide the daily necessities. While providing the exemption for RREP with respect to the development rights, the exemption provides the following :

- a. Special rate of tax of 5% to the commercial units.
- b. Exemption to the levy of supply of development rights to the extent of area of residential apartments (subject to sale of residential units prior to completion)

The special rate of tax to the commercial units is welcomed, however such rate of tax is burdened with the cost of the tax to be paid on the development rights procured for the commercial area which is not even eligible as ITC. We request you to extend the exemption of residential units to such commercial units in RREP too.

5. GST on Re-Development and Rehabilitation Projects

Another model more often used by developer is re-development of old building (or rehabilitation of slums) wherein existing members are allotted units and balance inventory is available for sale to the developer. Given the number of buildings reaching limits of structural safety increasing day by day, this model is very much prevalent in cities having old buildings/ structures and lack of space for horizontal expansion.

Till 31st March 2019, the Developer used to act as a works contractor for the existing members and charging them GST at 18% on the construction activity only. For the new customers buying units in such re-developed properties were subject to regular GST at effective rate of 12% after considering abatement for land component. However, under the revised GST scheme (effective from 1st April 2019), the notifications suggest that all such units given to existing members would be subject to

GST at par with units given to new customers taking into consideration the value of similar units. Since the value of land is embedded in the value of units given to new customers and the same being considered as the value for existing members, the existing members are required to pay higher amount of GST even when they only receive works contract service.

- A. We request your good self to provide a suitable clarification and allow correct treatment to be given to construction services which are in the nature of works contract when provided to existing members.
- B. We do also request the government to reduce the GST rate on all the new units in redevelopment (old/dilapidated structures) and all rehab schemes / Slum Rehabilitation schemes from 5% to 1% as such activity of builders is a socio-economic one for the benefit of the society and helping to achieve the vision/motto of the government of "Housing for All".

Why are we seeking this benefit?

With the lack of space being a major concern today, many cities are looking out for re-development of existing structures. In this process, the anomaly created by the revised GST scheme has completely halted the re-development projects wherein the existing member is made to face brunt of additional GST burden. Relief by way of clarification will again bring the stalled projects to work and move them towards completion. This will also help to bring the labour class back to employment in cities like Mumbai, Pune wherein such projects are at the forefront.

Such taxation on the development rights and the units provided to the existing landowners amounts to double taxation since the cost of construction of such units is the land cost to the developer which is also considered as output of the developer. Such equation of input as output results in rendering the project non-feasible. We request you to consider an exemption on transfer of development rights with respect to the Redevelopment projects.

6. Definition of Affordable Residential Units Needs Attention

The revised GST scheme has brought in a new definition of affordable housing. Presently, a dual threshold of INR 45 lakhs and carpet area of upto 90 sqm (in non-metropolitan cities/towns) or 60 sqm (in metropolitan cities) has been prescribed for the lower GST rate of 1% to apply on affordable housing units.

The cost of a 60 sq.mtr. house in Mumbai Metropolitan Region (MMR) area will always be above Rs.45 lakhs due to high land prices. None of such houses within MMR shall qualify for concessional rates of 1%. This makes the relief illusory to citizens of MMR.

It is therefore recommended that either there should be no value cap whatsoever at all or else, limit of Rs.45 lakhs to qualify for affordable house be raised to :

- **Rs.1.5 crores for Mumbai (MCGM limits) and Thane;**
- **Rs.1 crore for the rest of MMR.**

Further, the area threshold for metropolitan cities may also be increased from 60 sqm to 90 sqm, and for non-metropolitan cities from 90 sqm to 120 sqm in line with the PMAY Credit Linked Subsidy Scheme as also the current market and consumption trends. This shall ensure that the Indian population enjoys the benefit of reasonable and quality housing choices under the affordable housing scheme.

7. Reduction in GST Rate of Key Inputs and Input Services

At present, affordable housing is subjected to GST at 1% and other housing is subjected to GST at 5%. However, unlike all other goods and services the benefit of input tax credit is denied to the sector. It is in this context that GST rates on the procurement side becomes relevant for this sector. GST rates on some of the different types of inputs and input services are as follows :

Particulars	Present GST rates
Cement	28%
RMC, steel, flooring, doors and windows	18%
Electrical, plumbing, sanitary items	18%
Labour charges/ Services	18%

Specifically, cement constitutes a major component of construction cost (almost 10-15%) for any real estate project. Similarly, rate of labour and contract services is currently 18%.

Both these rates need a re-think as they are a major part of the cost of construction. Also, the fact that cement is the major raw material for all infrastructure projects, reducing its rate will also boost the infrastructure development and reduces its cost to the Government (who is the ultimate recipient of services in case of infrastructure projects).

Current rate of works contract services for government projects is 12% and hence a similar rate should also be given to real estate sector (for all the labour services it receives) that is also a contributor to the overall infrastructure development of the country.

In line with the current rate of works contract services for government projects which is 12%, we are also requesting for reduction in GST rate on contractors (works contract services for construction of building) from 18% to 12%, that would go a long way to reduce the overall cost of houses.

8. GST Rate of Construction Services Provided by Developer to Landowner Under a Joint Development Agreement and Consequent Credit Eligibility in the Hands of the Landowner

In an area share joint development agreement ('JDA') transaction, the developer is required to charge GST on construction activity carried out for the landowners.

As per the literal interpretation of Notification 3/2019, a developer-promoter should be eligible to apply the lower rate of 5%/ 1% (without input tax credit) on construction of apartments for the landowner. It appears that the intention of allowing input tax credit to the landowner (of such GST charged by the developer) is to ensure that the effective GST payable on landowner's share of units should be same as that of the GST paid by developer on sale of units to developer's customers.

However, there is an overall ambiguity as all the 5%/ 1% entries (inserted through Notification 3/2019) mention that para 2 (of Notification 11/ 2017) shall apply for valuation of this service.

While, for the purpose of valuation of service provided by a developer to landowner,

a specific valuation mechanism has been prescribed under para 2A.

It is therefore requested that a clarification be issued that developer will be liable to pay GST @ 5%/ 1% on construction activity carried out for the landowner and Landowner will be eligible to utilize the ITC of GST charged by the developer, for payment of output GST liability arising on further supply of under-construction apartments by the landowner.

As per the Notification No. 6/2019-CTR, the developer-promoter is required to pay GST at the time of issuance of completion certificate. However, the land owner-promoter may be required to pay GST in accordance with the provisions of Time of Supply earlier than issuance of completion certificate i.e. before the day on which developer-promoter would pay GST in respect of supply of construction of land owner-promoter. In such circumstances, which is bound to happen in almost all cases, that land owner-promoter will have to pay GST in cash at the time of supply and avail credit subsequently. It may also result in permanent non-utilization of input tax credit availed subsequently in hands of land owner-promoter resulting into doubling of taxation.

Developer-promoter shall be entitled to, without taking an obligation to, pay GST in full or part of the amount of GST liability prior to the time specified in Notification No. 6/2019, in as much and to the extent land owner-promoter is under an obligation to pay.

9. Benefit of ITC Should be Extended to Commercial Developments for Leasing or Leasing Rate be Reduced to 12%

ITC on inputs and input services used in construction of an immovable property is restricted as per section 17(5)(c) and 17(5)(d) of the Central Goods and Services Tax Act, 2017 ('CGST Act'). The language in the provision appears to suggest that the restriction shall apply to commercial developments meant for sale; while from an intention and parity in taxation standpoint, the benefit of input tax credit ought to be extended to commercial developments for sale as well as lease; given payment of full GST on the output side.

Denial of input tax credit implies increase in cost of doing business and investments becoming non-lucrative, thereby forcing developers to pass such additional tax cost to the lessees by way of increase in lease rental charges.

In a writ petition filed by M/S Safari Retreats Private Limited on this issue, the Hon'ble High Court of Orissa has held that GST input tax credit of goods and services used for construction of buildings intended for lease should not be restricted by provisions of section 17(5)(c) and 17(5)(d) of CGST Act. The ruling further holds that, any such restriction would need to be appropriately read down on grounds of parity in taxation (of properties meant for lease and those sold under construction) as well as to enable unfettered trade and commerce.

It is therefore requested that a suitable clarification may be issued, that the restriction from credit eligibility (of construction and works contract services except to the extent of those used for similar output services), under section 17(5)(c) and 17(5)(d) of the CGST Act, is not applicable for commercial developments for lease, taking into account the output GST being paid on such rentals.

10. Cancellation of Residential/Commercial units

As per present provisions, in case a unit is booked during the project implementation and gets cancelled say after September of subsequent year, then the mechanism for GST refund/adjustment is very tedious and precludes the benefit of GST paid if the cancellation occurs after the time limit under Section 34 of September of the following year in which services were rendered. Article 366(12A) defines "Goods and Services Tax" to mean any tax on the supply of goods or services or both. Hence there can be no GST when there is no supply of any goods or services. However, this fundamental principle itself is given a go-by, where a buyer cancels out on the flat after say three years of its construction. Given that the flat has been cancelled and the consideration for the same refunded along with the GST component, there is neither any "supply" nor any "consideration". Despite that being so, the assessee cannot issue a credit note and adjust its tax liability in the subsequent month because the outer time cap of "September following the financial year in which the services were rendered" has already been exceeded. Moreover, they cannot seek a refund of the GST paid on the cancelled flat, under Section 54 either, because the two years' time gap provided for under Section 54(1) has also been exceeded for no fault of the Developer. These aspects have been elaborated upon with the aid of the following illustration:-

- a) Suppose construction commenced on July 2017 and the flat was continuously constructed thereafter.
- b) The Financial Year in which construction commenced would be 1.04.2017 to 31.03.2018 (2017-18).
- c) Suppose the construction kept happening but the buyer suddenly cancelled out on the flat in July 2020.
- d) For the year 2017-18, credit notes cannot be raised for all the months from July 2017 to March 2018 because outer time limit of raising the same by "September 2018" has already been exceeded.
- e) For the year 2018-19, the Developer still cannot raise any credit notes from April 2018 to March 2019 because again the outer time limit of "September 2019" has already been exceeded.
- f) It is only in the year 2019-2020, that the Developer can raise credit notes for the months from April 2019 to July 2020 because it is only for this period that the outer time limit of "September 2020" has not been exceeded.
- g) Given that the developer cannot raise credit notes for all the months from July 2017 to July 2020 the Developer would have no option, but to file for refund claims under Section 54. Out of the claims so filed, those for the months of July 2017 to June 2018 would be time barred as being filed beyond the prescribed period of two years under Section 54(1).
- h) Therefore, as far as the months of July 2017 to July 2017 are concerned, the developer can neither issue a credit note under Section 34, nor file for a refund under Section 54.

Hence it is requested to have a mechanism to allow re-credit on unit which get cancelled without any specific time lime being the projects are running in years.

11. New GST return mechanism

We are aware that the new GST mechanism is coming into effect from Q3 of FY 2019-20. We understand that the new mechanism will have different methodology of filing GST returns. It may be noted that the real estate industry (especially residential

projects) to a major extent is out of input credit stream. However, the recently amended scheme for real estate players allows ongoing project to avail and continue the old scheme wherein input credit was available. Most of these projects would run in for about a year. Since the industry is used to the old return filing mechanism, we request you to please continue the same till March 2020. By this time, majority of the projects which opted for old scheme would be over. Effective April 2020, the industry would be focused on new set of compliances only for new projects.

There should also be a mechanism to allow refund of unutilised ITC as huge amount of money has got stuck in unutilised ITC or there should be a provision to allow offset of unutilised ITC against GST payable on projects under the new regime.

Lastly, changing the GST compliance mechanism in middle of the financial year would also make life difficult to maintain reconciliations and prepare annual returns and audits using two different sets of compliance modules. In light of the above, we request you to please implement the new return mechanism from the start of the next financial year.

IN SUMMARY

All our submissions above are aimed at fulfilling the vision and aspirations of the Government of India. By taking into consideration the above representation, the Ministry is only going to further show its commitment in solving the current financial situation and taking the economy on the path of \$5 Trillion.

We would be happy to discuss this in further detail with the fitment committee of the GST Council and concerned officials so that notifications to be released in this regard are in alignment with the thought process put forth by us.

We once again thank you for providing us an opportunity to put forth our concerns for the industry and the country as a whole.

Thanking you,

Your sincerely,
For CREDAI-MCHI



Nayan A. Shah
President



Bandish Ajmera
Hon. Secretary



Sanjiv S. Chaudhary MRICS
Chief Operating Officer