Taxation of JDAs – Clarity Needed!

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Finance Act 2017 amended the provisions of section 45 by inserting sub-section (5A) with effect from 1st April 2018 i.e. assessment year 2018-19. Sub-section (5A) provides that in case of an assessee being Individual or Hindu Undivided Family, who enters into a Joint Development Agreement/Specified Agreement, Capital Gains shall be chargeable as income of the previous year in which the certificate of completion for the whole or part of the project is issued by the competent authority. The said sub-section in effect defers the chargeability of the gain till the completion of the project. This deferment is no doubt subject to certain conditions mentioned in the sub-section. Sub Section (5A) further provides that the stamp duty value of the **share** of the assessee, in land or building or both, in the project on the date of issue of said completion certificate as increased by monetary consideration received, if any, shall be deemed to be the full value of consideration in terms of section 48 of the Act.

This sub-section has many interpretational issues but the subject matter of this article is only the controversy surrounding the phrase ‘share of the assessee’.

The computation of capital gains is based on two variables i.e. the sales consideration and cost of acquisition. The cost of acquisition would be the actual cost or the fair market value as on 1st April 2001. As far as the consideration is concerned, the Legislature in its wisdom thought it fit to link the consideration to the stamp duty value plus any actual receipt of monetary consideration in order to avoid disputes on what constitutes ‘full value of consideration’. As per the section the stamp duty value of the ‘share of the assessee’ in the land or building or both needs to be considered for the purposes of computing the consideration. Here is where the controversy kicks in; what is meant by the phrase ‘**share of the assessee**’. In common parlance consideration is what a person receives for giving up of something. Therefore, it is imperative to understand what is being ‘given up’ and what is ‘being received’ for the purposes of this sub-section so that the ‘share of the assessee’ can be correctly determined.

In many large projects the whole land is first transferred by the landowner to the developer and in lieu of which the landowner gets a share of the developed portion of the project. If the ratio agreed between the landowner and developer is 60:40, then the landowner is getting 60% of the developed project in lieu of giving up 100% of the land. In such a scenario the consideration would be the stamp value of 60% of the project (including the value of land) that is being received by the landowner. However, if in a case, where the full land is not being transferred like in individual housing collaboration agreements what would be the stamp duty value of the share of the assessee is the question. In a case where the landowner transfers 25% of the undivided portion of the land and receives three built up floors, ideally and logically the consideration should be the value of the built up three floors that the assessee is receiving (without considering the land value as land is already owned by the landowner).

Taking the above example but considering that the full land is transferred first and the landowner thereafter gets three built up floors, the consideration in this case for the landowner would significantly increase as it would now also include the stamp duty value of the undivided portion of the land. The department would therefore like to adopt this method of calculation as the tax payable is much higher though in both options the landowner would be the owner of three floors.

Let us try to understand the implications under both the above scenarios by taking an example. In order to appreciate the controversy one would also need to consider the computation hitherto insertion of sub-section (5A) of section 45.

Let us assume that Mr. A owns a plot of land. He enters into a collaboration with a builder 'B' who would construct 4 floors at his own cost and would retain one floor in lieu of the construction done by him for Mr. A. The Builder in addition to constructing the four floors (three for Mr. A), also pays a sum of Rs 1,00,00,000/- to the land owner Mr. A. The other facts are given below:

Cost of Construction of each floor: Rs 50,00,000/-

Undivided portion of land given up by Mr. A: 25%

Undivided portion of land retained by Mr. A: 75%

Stamp duty value of entire plot of land as at the date of sale: Rs 5,00,00,000/-

Stamp duty value of construction of each floor: Rs 30,00,000/-

FMV of land as at 1st April 2001: Rs 25,00,000/-

Computation as per normal provisions of Section 45 i.e. without considering 45(5A)

Sale consideration in its ordinary parlance would mean what is being received by the transferor. In case of a collaboration, the land owner gets constructed floors in lieu of giving up a certain portion of land in favour of the builder together with some monetary consideration. The aggregate value of the cost of construction plus the monetary consideration received thus becomes the full value of consideration. This consideration however needs to be tested for applicability of section 50C and if the stamp duty value as per section 50C is higher than the aggregate value of construction cost plus monetary consideration, it would be the stamp duty value that would be taken as the full value of consideration.

Particulars	Amount (Rs)
Sale Consideration- higher of (A) or (B): (A) Cost of construction of three floors: Rs.1,50,00,000 Monetary consideration: Rs.1,00,00,000 Total (A): Rs.2,50,00,000 (B) Stamp duty value of 25% of land: Rs.1,25,00,000 Total (B) : Rs.1,25,00,000	

Higher of (A) and (B)	2,50,00,000
Less: cost of acquisition of 25% of the plot of land as 75% is being retained by the land owner	6,25,000
Capital gains	2,43,75,000

Note: The above computation ignores indexation and the benefit of deductions under section 54/54F as the case may be.

Now let us compare the computation of capital gains basis the two methods of computation as explained hereinabove if the case is covered under section 45(5A):

Computation of capital gains where full land is transferred and then three floors are being returned to Mr A. (ignoring indexation for simplicity):

This option presupposes that the entire land is first being transferred and the landowner is getting 75% of the share (including the land value) back.

The computation is as under:

Particulars	Amount (Rs)
Sale Consideration- 75% of stamp duty value of land plus 75% of stamp duty value of construction plus Rs 1,00,00,000	5,65,00,000
Less: cost of acquisition of the full plot of land	25,00,000
Capital gains	5,40,00,000

Computation of capital gains where entire land is not transferred but only undivided portion of the land is transferred

In such a case, the computation will be based on the share in the project which is coming in i.e. only the stamp duty value of the constructed portion i.e. built up three floors and therefore the computation will be as under:

Particulars	Amount (Rs)
Sale Consideration- stamp duty value of 75% of the construction plus Rs 1,00,00,000	1,90,00,000
Less: 25% of cost of acquisition of the plot of land (25% of FMV as at 1st April)	6,25,000
Capital gains	1,83,75,000

It may be noted that since section 45(5A) deems the full value of consideration to be the stamp duty value of the share of the assessee as increased by the monetary consideration received, section 50C would not be applicable. In a case where 45(5A) is not applicable, only then would section 50C be applicable as the full of consideration would have to be tested for the value as per Section 50C.

Analysis and Conclusion

As can be seen from the above computation, there is a huge difference between the two methods of calculation under section 45(5A) and the tax authorities may like to adopt the first method in all cases irrespective of whether the land in full is being transferred in the first instance or not as it results in a higher tax outflow. Therefore, the way the JDA is drafted will have a huge role to play in the manner of computation of capital gains.

The final word on this will only be known once the matter is decided by the Courts and therefore till that time the taxpayers should be ready to litigate the matter should it be challenged by the authorities. However, to avoid this needless litigation it is suggested that necessary legislative changes are made to Section 45(5A) in the ensuing Budget session.