Taxability of Real state developers and Joint development agreement (JDA)

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Index

1. **Taxability in relation to transaction other than JDA**
   - Revenue Recognition as per ICDS III
   - Revenue Recognition as per ICDS IV

2. **Taxability in relation to Joint Development Agreement (JDA)**
   - Taxability in the hands of owner

3. **Penalties for Cash Transaction**
   - 269ST
   - 269SS

Taxability in relation to transaction other than JDA

Revenue Recognition when transaction is covered under AS7/ICDSIII

Revenue Recognition when transaction is covered under AS7/ICDSIII

Definition of Construction Contract

"Construction contract" is a contract specifically negotiated for the construction of an asset or a combination of assets that are closely interrelated or interdependent in terms of their design, technology and function or their ultimate purpose or use and includes :

(i) contract for the rendering of services which are directly related to the construction of the asset, for example, those for the services of project managers and architects;

(ii) contract for destruction or restoration of assets, and the restoration of the environment following the demolition of assets.

Revenue Recognition when transaction is covered under AS7/ICDSIII

Method of Calculation – Percentage of Completion Method

Under this method, contract revenue is matched with the contract costs incurred in reaching the stage of completion, resulting in the reporting of revenue, expenses and profit which can be attributed to the proportion of work completed.

Progress payments and advances received from customers or payment in advance to sub-contactors are not determinative of the stage of completion of a contract.

During the early stages of a contract, where the outcome of the contract cannot be estimated reliably contract revenue is recognised only to the extent of costs incurred. The early stage of a contract shall not extend beyond 25% of the stage of completion.

Revenue Recognition when transaction is covered under AS7/ICDSIII

Let's understand with an illustration how to recognise revenue

1

Contract Price (Sale Consideration)	1,000 lakhs
Estimated project cost	600 lakhs
Cost incurred till end of 1st year	120 Lakhs
At the 1st year end, enterprise will recognise revenue upto 120 lakh i.e. cost incurred till date as project is 20% completed [120/600*100] (i.e. less than 25%)	

2

Contract Price	1,000 lakhs
Estimated project cost	600 lakhs
Cost incurred till end of 2nd year	180 lakhs
At the 2nd year end, enterprise will recognise revenue as 180 [1000*30% - 120] as project is completed upto 30% (i.e. beyond early stage of 25%)	

Revenue Recognition when transaction is covered under AS7/ICDSIII

Applicability of ICDS III

ICDS III – Construction Contracts applies the determination of income of a contractors only arising from construction contracts.

Also, the definition of Construction contract (discussed earlier) clearly suggests that the construction undertaken by Real Estate Developers does not satisfy the above definition as the contract is not negotiated only for the construction of asset rather the Real Estate Developer is a person who constructs the asset as per his own schemes and designs and contracts with the buyer to sell the assets.

Revenue Recognition when transaction is covered under AS7/ICDSIII

Applicability of ICDS III

Guidance Note on ICDS issued by ICAI also states that the ICDS III is not applicable to real estate developers.

CBDT has also clarified vide Circular No 10/2017, *"present there is no specific ICDS notified for real estate developers, BOT projects and leases. Therefore, relevant provisions of the Act and ICDS shall apply to these transactions as may be applicable."* Therefore, CBDT has tacitly accepted that ICDS III not applicable to Real Estate Developers

Revenue Recognition In case of

Construction Contractors

As per ICDS III/ AS 7

Real Estate Developers

As per AS9/ ICDS IV Guidance note of ICAI on Real Estate Developers

Revenue Recognition In Case of Real Estate Developers

Revenue Recognition in case of Real Estate Developers

ICDS IV – Revenue Recognition

As per ICDS-IV, in a transaction where the sale of goods is involved, the revenue shall be recognised when the seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership.

In case of transaction between a developer and buyer, at what point in time does all significant risks and rewards of ownership can be considered as transferred?

Guidance Note on Accounting for Real Estate Transactions

Steps prescribed to recognise revenue for real estate transaction

1	2	3
Verify whether risk and reward had been transferred or not	Verify whether conditions to recognise revenue had been fulfilled or not	Now, recognise revenue as per the method prescribed in Guidance Note

Revenue Recognition in case of Real Estate Developers

Step 1: Risk and Reward Transfer

In case of real estate sales, the seller usually enters into an agreement for sale with the buyer at initial stages of construction. This agreement for sale is also considered to have the effect of transferring all significant risks and rewards of ownership to the buyer provided the agreement is legally enforceable and subject to the satisfaction of conditions which signify transferring of significant risks and rewards even though the legal title is not transferred or the possession of the real estate is not given to the buyer.

Once the seller has transferred all the significant risks and rewards to the buyer, any acts on the real estate performed by the seller are, in substance, performed on behalf of the buyer in the manner similar to a contractor.

Accordingly, revenue in such cases is recognised by applying the percentage of completion method on the basis of the methodology explained in AS 7, Construction Contracts

Example

Developer **Buyer**

Developer made an sale agreement on 01.01.2022 with buyer

Developer started construction of property on 01.01.2022 and construction continues till 31.12.2024

After completion i.e. as on 01.01.2025 developer give possession of house to buyer

Some of the conditions of agreement to sale to confirm that risk and rewards are transferred are as below

1. Developer retains no effective control of the property usually associated with ownership.

2. Possession of property effectively transferred to buyer

3. No significant uncertainity exist regarding the amount of sales consideration

4. No uncertainity exists regarding collection of sales consideration

Revenue Recognition in case of Real Estate Developers

Step 2: Conditions to recognize revenue

Condition 1

All critical approvals necessary for commencement of the project have been obtained. These include, wherever applicable:
(i) Environmental and other clearances.
(ii) Approval of plans, designs, etc.
(iii) Title to land or other rights to development/ construction.
(iv) Change in land use.

Condition 2

At least 25% of the saleable project area is secured by contracts or agreements with buyers.

Condition 3

When the stage of completion of the project reaches a reasonable level of development, i.e., beyond 25 % of total construction and development costs of the project. Costs excludes – Land and Borrowing cost.

Condition 4

At least 10 % of the total revenue as per the agreements of sale are realised AND reasonable to expect that it shall be realised at the reporting date in respect of each of the contracts.

Revenue Recognition in case of Real Estate Developers

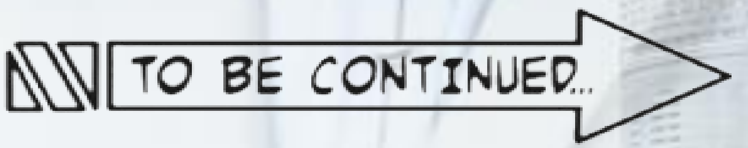
Step3

Let's understand with an illustration how to recognise revenue

Total saleable area	20000 sq. ft.
Estimated project cost (includes land cost Rs.300 lakhs and construction cost Rs.300 lakhs)	600 lakhs
Cost incurred till year end (includes land cost Rs. 300 lakhs and construction cost Rs. 60 lakhs) (Condition 3 not Satisfied)	360 lakhs
Total sales consideration of 5000 sq. ft. (Condition 2 Satisfied)	200 lakhs
Amount realised till year end (Condition 4 Satisfied)	50 lakhs
% of completion of work	60% of total project cost or 20% of construction cost
At the year end, enterprise will not able to recognise revenue as 25% of total construction cost will not achieved.	

Revenue Recognition in case of Real Estate Developers

Continuing with the previous illustration



Work completed till year end (includes land cost Rs. 300 lakhs and construction cost Rs.90 lakhs)	**390 lakhs**
% of completion of work (Condition 3 also satisfied)	**65% of total project cost or 30% of construction cost**
Now, enterprise will able to recognise revenue at year end as shown below:	
Revenue recognised (200 lakhs*65%)	**130 lakhs**
Proportionate cost (5000 sq. ft./20000 sq. ft.)*390	**97.50 lakhs**
Income from the project	**32.50 lakhs**
Work in progress to be carried forward	**292.50 lakhs**

Taxability in relation to transaction with JDA

What is JDA ?

JDA is an agreement executed between the Land owner and the Developer/Builder of a real estate project.

Whereby the owner of the land provides his land to a developer who undertakes the development/ construction of property and other related work

When the construction is completed, the developer might allot specified number of units to the land owner as per the mutually decided share or the land owner may receive percentage share of the consideration received from sale of the units.

This agreement may also give the Developer the rights to sell remaining flats to outsiders

Joint Development Agreement

Land Owner

Developer

Provides Land For Development

Share revenue from sale of Developed property or provide area in the Developed property

Various stages/ Transaction in JDA?

Stage 1: Land owner and developer enters into Joint Development agreement.

Stage 2: Developers completes the project and get’s completion certificate.

Stage 3: Land owner/ developer sells their respective share of units or Land owner could even sell his share of developed property before getting completion certificate.

Does any taxability arise when land owner and developer enter into an agreement?

Before Introduction of 45(5A)

Before introduction of Section 45(5A) normal provision of Capital gain would be attracted wherein we need to first check the provision of Sec. 2(47) i.e. 'transfer'.

Clause (i) - sale, exchange or relinquishment of the asset

Clause (ii) - extinguishment of any rights therein

Clause (vi) - any transaction which has the effect of transferring, or enabling the enjoyment of, any immovable property.

Clause (v) - any transaction involving the allowing of the possession of any immovable property to be taken or retained in part performance of a contract of the nature referred to in section 53A of the Transfer of Property Act, 1882.

Before Introduction of 45(5A)

Revenue is of the opinion that when Land owner has entered into JDA and allowed developer to take possession of his land for development, transfer as per "transfer of property act" has taken place and accordingly land owner has to pay tax on same even if no actual revenue has been earned by land owner at that point of time.

Decision in Support of such taxation:

(1)Charturbuj Dwarakadas Kapadia Vs CIT (2003) 260 ITR 491 (Bom)
(2)CIT is. Dr. T.K. Dayalu [2011] 202 Taxaman 531 - Kar. HC;
(3)ACIT vs. Ram Reddy (2012) 23 Taxmann.com 59-Hyd. ITAT;
(4)ITO vs. P.A. Sarala [2015] 154 ITD 168-Chen. ITAT;
(5)ITO vs. Dr. Arvind Goverdhan. (2018) 61 ITR(T) 159 (Bang. ITAT);

Before Introduction of 45(5A)

Further, there are various case laws which does not support the above contention of revenue or are against the above contention and consider the year of taxability as the year in which:

1. Consideration is actually received by land owner and not on the date of entering into JDA:

CIT vs. Smt. Najoo Dara Deboo [2013] 218 *Taxman* 473 *(All);*

Mrs. Aarti Sanjay Kadam vs. ITO [2018] 172 *ITD* 362 - *Mum. ITAT*

2. While entering into JDA developer only get's right to construct and asset is not transferred as possession is not transferred:

CIT vs. Shri Sadia Shaikh [2014] *Tax Appeals No.*11 & 12 *of* 2013 *(Bom. HC)*

CIT vs. Atam Prakash Sons [2008] 219 *CTR* 164 *(Del HC)*

C.S. Atwal vs CIT [2015] 378 *ITR* 244 *(P&H HC)*

K. Radhika vs. DCIT [2012] 149 *TTJ* 736 *(Hyd. ITAT)*

K.V. Satish Babu [HUF] v. Income-tax Officer [2023] 152 *taxmann.com* 396 *(Bangalore - Trib.)*

After Introduction of 45(5A)

Section- 45(5A)

Notwithstanding anything contained in sub-section (1),

- **where the capital gain arises to an assessee, being an individual or a Hindu undivided family,**

- **from the transfer of a capital asset, being land or building or both, under a specified agreement,**

- **the capital gains shall be chargeable to income-tax 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; and**

- **for the purposes of section 48, the stamp duty value, on the date of issue of the said certificate, of his share, being land or building or both in the project, as increased by the consideration received in cash, if any, shall be deemed to be the full value of the consideration received or accruing as a result of the transfer of the capital asset:**

Section 45(5A)- Proviso

Provided that the provisions of this sub-section shall not apply where the assessee transfers his share in the project on or before the date of issue of the said certificate of completion, and

- **the capital gains shall be deemed to be the income of the previous year in which such transfer takes place and**

- **the provisions of this Act, other than the provisions of this sub-section, shall apply for the purpose of determination of full value of consideration received or accruing as a result of such transfer**

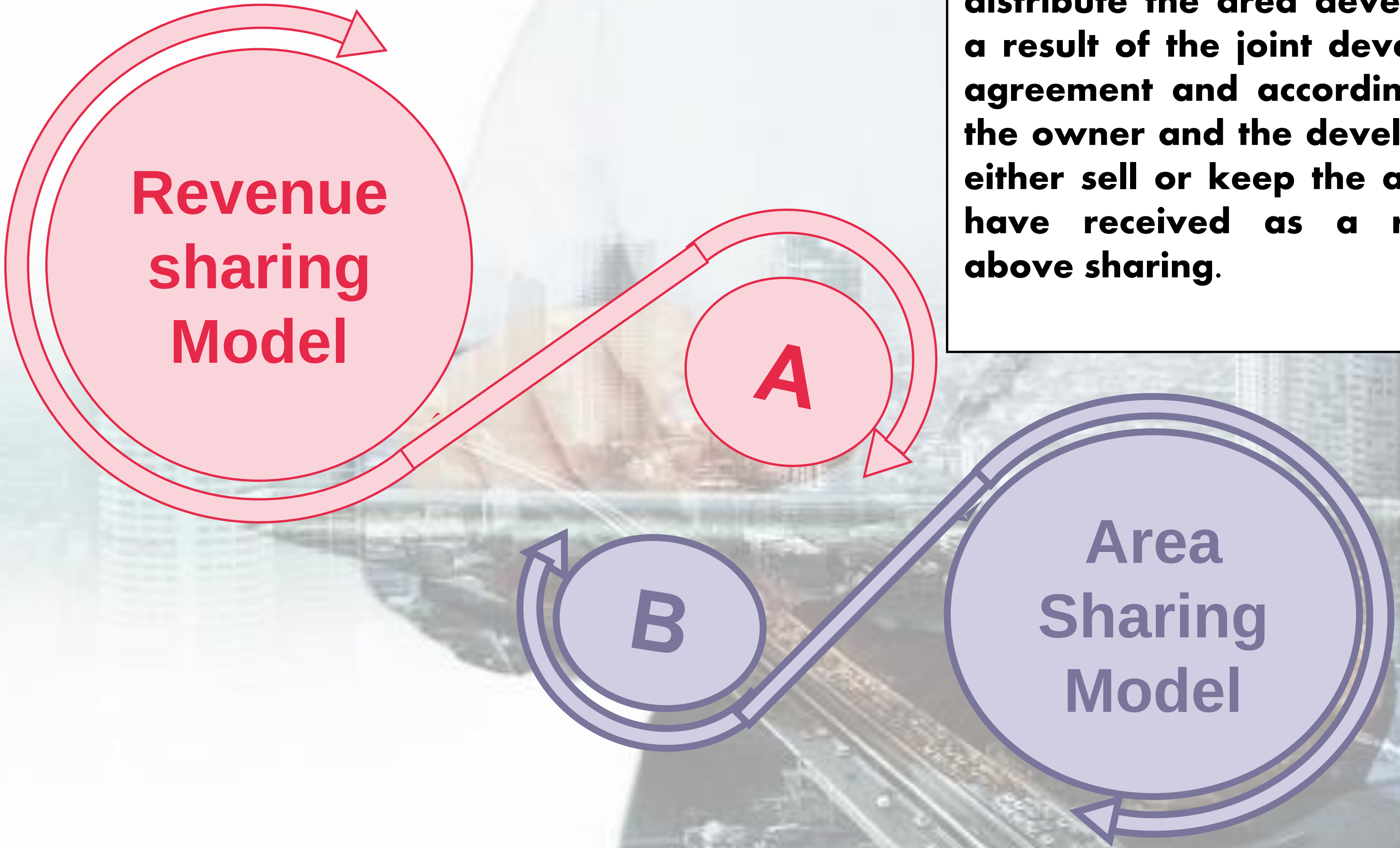
Explanation.—For the purposes of this sub-section, the expression—
(i) "competent authority" means the authority empowered to approve the building plan by or under any law for the time being in force;
(ii) "specified agreement" means a registered agreement in which a person owning land or building or both, agrees to allow another person to develop a real estate project on such land or building or both, in consideration of a share, being land or building or both in such project, whether with or without payment of part of the consideration in cash;
(iii) "stamp duty value" means the value adopted or assessed or assessable by any authority of the Government for the purpose of payment of stamp duty in respect of an immovable property being land or building or both.

Types of JDA Model

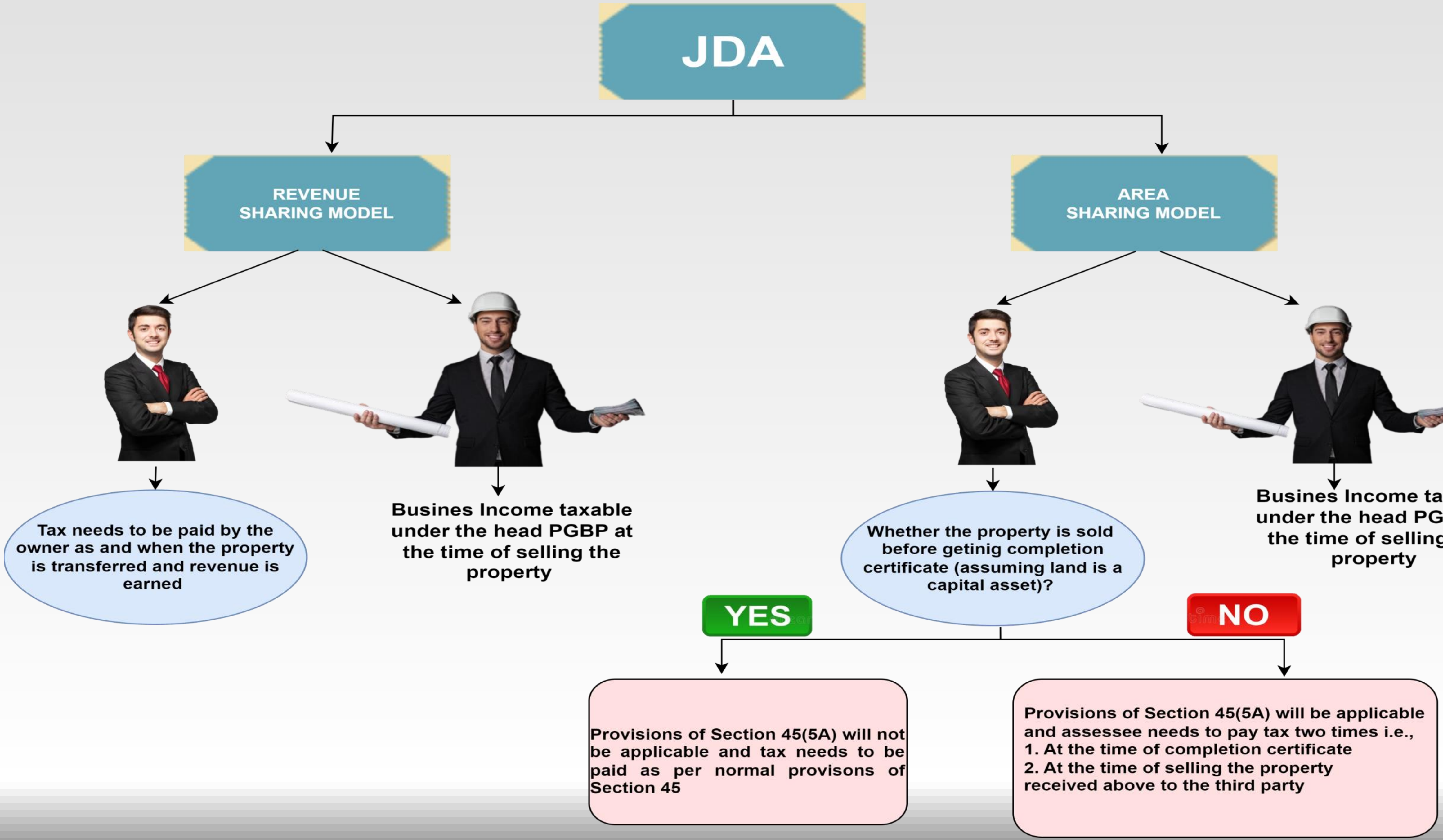
Arrangement to share the proceeds arising from the development of immovable property belonging to the Land Owner.

Under these agreement/ arrangements

i. The Land Owner and Developer agree to share the "Distributable Revenue" in a specified percentage. The term "distributable revenue" is specifically defined in the development agreement apart from other terms and conditions



Under this arrangement, the land owner and the developer decides to distribute the units which will be developed, or they agree to distribute the area developed as a result of the joint development agreement and accordingly both the owner and the developer can either sell or keep the area they have received as a result of above sharing.


JDA
REVENUE SHARING MODEL
AREA SHARING MODEL
Tax needs to be paid by the owner as and when the property is transferred and revenue is earned
Busines Income taxable under the head PGBP at the time of selling the property
Whether the property is sold before getinig completion certificate (assuming land is a capital asset)?
Busines Income taxable under the head PGBP at the time of selling the property
YES
NO
Provisions of Section 45(5A) will not be applicable and tax needs to be paid as per normal provisons of Section 45
Provisions of Section 45(5A) will be applicable and assessee needs to pay tax two times i.e.,
1. At the time of completion certificate
2. At the time of selling the property received above to the third party

How to Calculate Capital gain?

Under section 45(5A)

Under the provision of Section 45(5A) it is very clear that the stamp duty value of the property received by the land owner shall be the sale consideration for the land owner along with cash consideration received if any.

Capital gain under other provision of the Act

If the assessee is not getting covered under the provisions of Section 45(5A) in such case also assessee can consider the Stamp duty value of property on date of transfer along with cash receipt if any, as sale consideration

Cost of acquisition

The cost of Land needs to be distributed amount the area of flats which he has received as consideration while calculating Capital gain income.

Let's understand it with an example

Mr. A owns a land worth Rs. 10 lakh which he was holding from 2010. Now in 2020 he entered into a JDA to receive 4 flats against his land and accordingly the cost of Rs. 10 lakh will be distributed among 4 flats to calculate Capital gain.

Is there any exemption from the capital gain arising out of JDA?

If the asset sold by assessee is a capital asset and the asset was held for Long term purpose, then assessee can claim below mentioned exemption against such Capital gain income.

Long Term Capital Gains Tax Exemptions on Sale of Land / House

	Section 54	Section 54EC	Section 54F
Who can claim the exemption?	Individual / HUF	Any person	Individual / HUF
Asset sold / transferred	Residential Property	Any long term capital asset	Land / Plot (other than Residential house)
Holding period of Original Asset	3 years	3 years	3 years
New Asset to be acquired	Residential house	Notified Bonds	Residential house
Time limit for new investment	Purchase : 1 year backward or 2 year forward. Construction : 3 years forward.	within 6 months	Purchase : 1 year backward or 2 year forward. Construction : 3 years forward.
Exemption Amount	Investment in the new asset or capital gain, whichever is lower	Investment in the new asset or capital gain, whichever is lower (max Rs 50 Lakh)	(Long Term Capital Gain * Amount invested in new house) divided by Sale proceeds of original asset ie Net consideration

Section 194IC

Payment under specified agreement

194-IC. Notwithstanding anything contained in section 194-IA, any person responsible for paying to a resident any sum by way of consideration, not being consideration in kind, under the agreement referred to in sub-section (5A) of section 45, shall at the time of credit of such sum to the account of the payee or at the time of payment thereof in cash or by issue of a cheque or draft or by any other mode, whichever is earlier, **deduct an amount equal to ten per cent of such sum as income-tax thereon.**

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What will happen if JDA is not registered?

CIT vs. Balbir Singh Maini [2017] 398 ITR 531 (SC)

Vide the Registration and Other Related Laws (Amendment) Act, 2001, amendments were made simultaneously in Section 53A of the Transfer of Property Act and Sections 17 and 49 of the Indian Registration Act.

- The effect of the aforesaid amendment is that, on and after the commencement of the Amendment Act of 2001, if an agreement, like the JDA, is not registered, then it shall have no effect in law for the purposes of Section 53A.

- This being the case, in order to qualify as a "transfer" of a capital asset under Section 2(47)(v) of the Act, there must be a "contract" which can be enforced in law under Section 53A of the Transfer of Property Act.

- A reading of Section 17(1A) and Section 49 of the Registration Act shows that in the eyes of law, in the absence of registration, there is no contract which can be taken cognizance of, for the purpose specified in Section 53A.

Whether tax will be applicable if POA is given to developer to develop the land?

Seshasayee Steels (P.) Ltd. vs. ACIT [2020] 421 ITR 46 (SC)

Questions before Supreme Court:

- **Whether provision of Section 2(47)(v) gets attracted considering the 'agreement to sell' & 'power of attorney' and accordingly taxability will be in AY 1998-99 and not AY 2004-05?**

- **Whether provision of section 2(47)(vi) gets attracted considering agreement to sell and POA as 'enabling the enjoyment of any immovably property' and accordingly taxability will be in AY 1998-99 and not AY 2004-05?**

- **Whether 'Memo of Compromise' can in anyway attract any of the clause of Section 2(47)?**

Whether tax will be applicable if POA is given to developer to develop the land?

Observations/ Extract from Hon'ble Supreme court judgement:

- In order to attract provision of Section 2(47)(v), provision of Section 53A of TOPA, 1882 needs to be fulfilled.

- As per the agreement to sell only a licence was given to the builder upon the land for the purpose of developing the land into flats and selling the same.

- Such license cannot be said to be 'possession' within the meaning of Section 53A, which is a legal concept, and which denotes control over the land and not actual physical occupation of the land.

- Since provisions of Section 53A of TOPA,1882 are not attracted here, hence even section 2(47)(v) cannot be attracted.

- Placing reliance on the decision of Hon'ble Supreme Court in case of CIT vs. Balbir Singh Maini [2018] 12 SCC 354 it was reiterated that the expression "enabling the enjoyment of" must take colour from the earlier expression "transferring". Accordingly, there needs to be transfer on account of extinguishment of the assessee's right over the property.

- It was pursuant to the 'deed of compromise' dated 19.07.2003 the assessee received the consideration (after certain reduction) in full and final settlement in respect of the 'agreement to sell'.

- Thus, assessee's rights in the said immovable property were extinguished on the receipt of the last cheque.

- The 'deed of compromise' dated 19.07.2003 could be stated to be a transaction which had the effect of 'transferring' the immovable property.

Case Study - 1

Facts of the case:

Mr. A is a Land owner owning a residential plot in Jhotwara. He was approached by a builder in 2017 wherein the builder offered to build a building on his land of 8 floors with 4 flats on each floor. The plan was finalized and JDA was signed and registered in December 2018.

As per the JDA agreement it was decided that out of the 32 flats 18 would belong to the Land owner and 14 would belong to the Builder.

It was decided that Building shall be completed and completion certificate shall be received till December 2023.

Now Mr. A has approached you to ask the below mentioned queries:

1. **What will be the tax implication i.e. Income tax and GST if he sell property before received the completion certificate?**
2. **How to calculate such capital gain?**
3. **Can he claim any exemption against such capital gain.**
4. **What will be the effect if land owner had converted such property into stock in trade in 2010**

Case Study - 2

Facts of the case:

Mr. A is a Land owner owning a residential plot in Jhotwara. He was approached by a builder in 2017 wherein the builder offered to build a building on his land of 8 floors with 4 flats on each floor. The plan was finalized and JDA was signed and registered in December 2018.

As per the JDA agreement it was decided that builder and land owner shall distribute revenue between them on each flat sold in the ratio of 60% to land owner and 40% to Builder.

It was decided that Building shall be completed and completion certificate shall be received till December 2023.

Now Mr. A has approached you to ask the below mentioned queries:

1. What will be the tax implication i.e. Income tax and GST if they decide to sell property before receiving the completion certificate.
2. How to calculate such capital gain?
3. Can he claim any exemption against such capital gain.
4. Will there be any change if they decide to change the method in between from revenue sharing to area sharing.

Case Study - 3

Facts of the case:

Mr. Z is a Land owner owning a residential plot in Jagatpura. He approached a developer in 2023 wherein he asked the developer to develop the land by levelling the land, putting drainage lines and other related things. Against the same the land owner offered him a part of such developed plot and accordingly both of them entered into a JDA agreement.

As per the JDA agreement it was decided that developer and land owner shall distribute developed plots between them and developer would get 20% of plots and owner would keep 80%.

Now Mr. Z has approached you to ask the below mentioned queries:

1. **What will be the tax implication i.e. Income tax and GST on the above transaction once they sell such plot.**
2. **How to calculate such capital gain?**
3. **Can he claim any exemption against such capital gain.**

Penalties for Cash Transaction in immovable property

269ST

Person shall receive an amount of two lakh rupees or more—

(a) in aggregate from a person in a day; or

(b) in respect of a single transaction; or

(c) in respect of transactions relating to one event or occasion from a person,

otherwise than by an account payee cheque or an account payee bank draft or use of electronic clearing system through a bank account or through such other electronic mode as may be prescribed

Provided that the provisions of this section shall not apply to—

(ii) transactions of the nature referred to in section 269SS

Kindly note that Limit of 269ST i.e. 2,00,000 only applies in case if transaction is not covered under 269SS

Let's see 269SS whether transaction of transfer of Immovable property is covered under 269SS or not?

269SS

No person shall take or accept from any other person (herein referred to as the depositor), any loan or deposit **or any specified sum**, otherwise than by an account payee cheque or account payee bank draft or use of electronic clearing system through a bank account or through such other electronic mode as may be prescribed, if,—

(*a*) the amount of such loan or deposit or specified sum or the aggregate amount of such loan, deposit and specified sum; or

(*b*) on the date of taking or accepting such loan or deposit or specified sum, any loan or deposit or specified sum taken or accepted earlier by such person from the depositor is remaining unpaid (whether repayment has fallen due or not), the amount or the aggregate amount remaining unpaid; or

(*c*) the amount or the aggregate amount referred to in clause (*a*) together with the amount or the aggregate amount referred to in clause (*b*),

is twenty thousand rupees or more:

"specified sum" means any sum of money receivable, whether as advance or otherwise, in relation to transfer of an immovable property, whether or not the transfer takes place.

As, 269SS applied to specified sum and definition of specified sum includes transfer of Immovable property.

Limit for cash transaction in immovable property is 20,000 and not 2,00,000

Thank You

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