Development in Joint Development Agreement

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Background of the Joint Development Agreement

The concept of Joint Development Agreement (JDA) is not new in India, especially metro cities and cosmopolitan cities. It is a fairly common arrangement for developers and builders to enter into development related arrangement with land owners rather than making an outright purchase of the land for their project. Land owners may grant right to develop their land under the agreement entered on mutually agreed terms and conditions. In other words, development right can be given by the following ways.

(a) Sole development agreement,
(b) Development service agreement,
(c) Joint development agreement.

Sole Development Agreement

Generally, in a sole development agreement, the developer makes an upfront payment in favour of the land owner which enables the developer to own the built up space on the land without having any ownership right in the land, which at all times vested in the hands of the owner. However, this is not a common arrangement between the land owner and the developer because in this arrangement, the developer has to give substantial amount to the land owner upfront which leads to huge cash flow. Further, in this arrangement, the developer has to bear all the risk till the end of such project. The agreement, in the case of sole development agreement, is drafted differently which in detail covers the risk and rewards and other terms and conditions.

Further also, the income tax is chargeable in the year of transfer of property i.e. in the year in which the such agreement entered into. The amendment introduced in this budget are for Joint Development Agreement and not for Sole Development Agreements.

Development Service Agreement

As far as development service agreements are concerned, the land owner gets the land developed by a developer against payment of fixed consideration. In such agreements, the developers only obligation is to develop the land and handover the developed land to the land owner. In other words, the developer acts like a contractor and get the remuneration for the service rendered.

Joint Development Agreement

The third category is the generally accepted option for real estate projects i.e. Joint Development Agreement (JDA). In JDA, the owner
provides the land free from all title defects and undertakes the development of such land along with the developer. In such arrangement, the land owner continues to own the land and shares the responsibility to develop the building along with developer. In such agreement, the basic work is to be done by the developer i.e. the man power, equipment, expertise and experience to implement the project. The agreement can be done in which the land owner and the developer either for sharing of sale proceeds or lease of the built up space or owning the built up space in the agreed ratio. In the first case, i.e. sharing of revenue from the built up space. It is the responsibility of the developer to develop the land jointly with the land owner and sell or lease the built up space to the third party and share the proceeds in the agreed ratio. Since the ownership is continues to be with the land owner, the developer would require the co-operation of the land owner to transfer the title in the name of the buyer. In such cases, the developer has the right for specific performance which shall be enforceable in the court of law if the land owner fails to co-operate with the developer.

**Tax provisions relating to JDA**

Before the Finance Bill 2017, the taxation authorities generally rely upon on the judgment of the Bombay High Court in the case of *Chaturbhuj Dwarkadas Kapadia of Bombay v. CIT* [2003] 129 Taxman 497 wherein it has been held that a taxable event emanates from the execution of a joint development agreement and it will be taxed in the year of execution of the said agreement.

Section 2(47)(v)/(vi) of the Income-tax Act, 1961 provides that "transfer" includes :-

(a) 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, or;

(b) any transaction by way of agreement or arrangement or in any other manner whatsoever which has the effect of transferring or enabling the enjoyment of any immovable property.

As per the provisions of section 45(1), any profit or gains arising from the transfer of capital assets effected in the previous year shall be chargeable to income tax under the head Capital Gain and shall be deemed to be the income of the previous year in which the transfer took place.

So, till now the position of the law to the tax the transfer of land is very clear and it will be taxed in the year of execution of the said agreement. While following this position of law, the problem arises that in many cases, in the instance of first transfer, the land owner enters into agreement and receive nominal amount for the shake of guarantee and not the full consideration of such land, however, while calculating tax liability, the full value of the land has to be taken as consideration. It creates lot of financial hardship on the landowner. At this juncture, it is
important to revisit the meaning of transfer of property as per Section 5 of the Transfer of Property Act, 1882. "Transfer of property" means an act by which a living person conveys property, in present or in future, to one or more other living persons. Now the question arises, what is the meaning of person conveys property. The conveyance is an act of transferring an ownership interest in real property from one party to another. By this discussion, it is clear that to consider the first instance a transfer is not correct because, it is a transfer only when the land owner transfers the ownership in the property.

Section 53A of the Transfer of Property Act, 1882 is about the part performance i.e. Where any person contracts to transfer for consideration any immovable property by writing signed by him which the terms necessary to constitute the transfer can be ascertained with reasonable certainty, and the transferee has, in part performance of the contract, taken possession of the property or any part thereof, or the transferee, being already in possession, continues in possession in part performance of the contract and has done some act in furtherance of the contract, and the transferee has performed or is willing to perform his part of the contract. These provisions of Section 53A has been considered in the judgement of Chaturbhuj Dwarkadas Kapadia of Bombay (supra) and further reiterated in many judgements.

**Change in the budget**

Through this budget, a new sub-section 5A inserted which says, 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.

This is very important change which nullify the Chaturbhuj Dwarkadas Kapadia of Bombay (supra) judgement and may other judgement which were pronounced in the same line.

Now the question arises, why this change has been introduced? As per the memorandum of the Budget, with a view to minimise the genuine hardship which the owner of land may face in paying capital gains tax in the year of transfer, it is proposed to insert a new sub-section (5A) in section 45.

The second change introduced by the CBDT through section 194IC which says 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.”.

Beside collection of tax, yet another objective sought to be achieved by inserting TDS provisions is the trail created for collection of tax due to
exchequer from the said transactions.

Impact of such changes

It is very simple to understand that the value of property will grow with the development of property. Earlier the tax was levied on the transfer of property before the property was developed which fetches the lower market value. Consequently, lower tax will be levied due to the lower sale consideration. Alternatively, post amendment, the higher amount of tax shall be charged in case of transfer of developed property due to increase in fair market value of such developed property.

Further, such change is applicable for the Individual and HUF. There is no reason, why other taxable entities, like Company, Firm, Cooperative of Group Housing Societies are not included for this benefit.

Further, it is also 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 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 as per the provisions of this Act. Now the question arises, whether the entire property is deemed to be transferred and taxed accordingly or only to the extent it is transferred. Because, as per the provision, sub section 5A shall not apply if the assessee transfer his share of property before the issue of certificate of completion.

In relation to deduction of tax, the proposal that any person paying to a resident any sum by way of consideration must deduct tax at source at 10% either at the time of credit of such sum to the account of the payee or at the time of payment, whichever is earlier. Through this deduction of tax, the trail of transaction can be recorded and 10% of the sum paid by way of other than kind is come to the Government kitty in advance. One good relief given in the context of tax deduction relates to confining the deduction to consideration paid in cash and excluding explicitly that TDS will not apply for consideration in kind.

Conclusion

To conclude, it can be said that it's a good move by the Government considering the fact that real estate sector is bleeding and now a day no developer wants to invest big chunk of his funds in purchase of land. With this amendment, the landowner will also not hesitate to enter into such agreement because tax pay out in the year of completion and completion certificate has been obtained by the authority. In relation to TDS, this kind of clarity in law will pave the way for better compliance and reduction in litigation.