Addendum to Agenda Item 5 (Recommendations of the GoM for boosting Real Estate Sector under GST regime) – Record of discussion of Fitment Committee held on 23/4/19.

The GST Council in its 33rd Meeting on 20th February, 2019 had directed that the Fitment Committee may work out the operational requirements and examine other issues raised by the States with regard to the recommendations of the GoM for boosting Real Estate, and to submit a report when the Council resumes the meeting on 24th February, 2019. The issues involved were examined by the Fitment Committee in its meeting held on 23rd February, 2019.

2. The views and suggestions of the Fitment Committee on issues related to each recommendation of the GoM are as under:

I. Rate of tax

GoM recommendations before the GST Council for consideration

- Effective GST @ 5% without ITC on non- affordable residential properties, and
- Effective GST @ 3% or less without ITC on affordable residential properties may be levied.

Fitment Committee's view:

Regarding affordable residential properties many officers felt that rate of 3% appears to be higher and effective rate of 1% without ITC would be appropriate.

II. Definition of affordable housing

GoM recommendation before the GST Council for consideration

Definition of affordable housing may be revised to, inter alia, include -

- The existing schemes of State and Central Government covered under GST notification No. 11/2017-Central Tax (Rate) dated 28th June, 2017.

  And
- An additional criteria of RBI's priority sector lending guidelines having financial limit of Rs. 30 lacs in non-Metro and Rs. 45 lacs in metro cities.
- Definition of metropolitan city to be examined as the definition for banking purpose is very wide.
- Existing affordable housing shall also pay tax as per the new rates for the remaining instalments.

Fitment Committee's suggestion:

Metropolitan Cities should include only Bengaluru, Chennai, Delhi NCR (limited to Delhi, Noida, Greater Noida, Ghaziabad, Gurgaon, Faridabad), Hyderabad, Kolkata, Mumbai (MMR).

III. Safeguards to maintain the integrity of supply chain and protect revenue

GoM recommendations before the GST Council for consideration

- Purchase of inputs, capital goods and input services other than TDR (or similar rights) from a GST registered supplier to be minimum 80% to maintain the integrity of the supply chain.
- Applicable tax rate on shortfall of purchases below this threshold limit will be on merit rate on RCM basis may be decided in the Fitment Committee

Issues raised by the States:

1. Issue: What should be the applicable rate on the shortfall to meet the condition of mandatory sourcing of 80% from registered person?

2. **Issue**: Which supplies should be subjected to GST under RCM, as merit rate across the supplies would vary, and the registered entity may simply opt to pay GST under RCM on the supplies attracting lowest GST rate.

Fitment Committee's suggestion:

(i) Tax rate on such shortfall may be fixed at flat rate of 18% with Cement as exception.

(ii) Cement, in case procured from unregistered person, shall be charged at 28% on RCM basis.

3. Issue: The inputs may be procured on basis of fake invoices etc to meet the mandatory purchase requirement. For properly ensuring integrity of the credit chain, the cap may be increased to 90%.

Fitment Committee Recommendations:

(i) The method of apportionment may be made through GSTR 3B to make it similar to ITC procedure.

(ii) Further, where supply has been shown to be received from a GST registered person who is non-existent, it shall be deemed that the purchase has been made from a non-registered person.

(iii) RCM payment to be done on pro-rata basis, every month, to be adjusted at the end of the year.

(Fitment Committee was of the view that the proposal may be simplified by shifting tax liability on all purchases from unregistered persons on the developers under RCM at the merit rate of each purchase.)

4. Issue: 80% limit should be applied only to building materials which go into the construction and should not include capital goods of the builder.

Fitment Committee' suggestion:

Capital goods to be procured only from registered person, and shall not be used for computing the 80:20 ratio (neither in numerator nor in denominator)

5. Issue: With regard to 80% mandatory sourcing, there is lack of clarity whether the requirement of 80% will be for a project or a registration.

Fitment Committee Recommendation:

80:20 ratio shall be verified for residential property at the end of the year and at the end of the project.

IV. Transitional provisions and detailing issues pertaining to mixed properties (residential and commercial) under proposed tax structure

GoM recommendations before the GST Council for consideration

- The proposed rate should apply only to the residential property.
- The ITC reversal methodology, i.e. ITC required to be reversed with respect of commercial units in a mixed property (residential and commercial) under proposed tax structure may be decided by the Fitment Committee.

1. Issue: Transition provisions for ongoing projects

Principles agreed upon by Fitment Committee:

(i) ITC shall be available only to the extent (calculated on pro-rata basis) of the value of the supply made out of the total value of supply for the project till the date of transition. ITC taken less vis-à-vis the supply made shall be

quantified and can be used to adjust the future tax liability. ITC taken in excess of supply made (calculated on pro-rata basis) shall be recovered.

(ii) The ITC with respect to work in progress and inputs lying in stock shall lapse.

(iii) The ITC balance lying in the ledger after paying the liability relating to supplies made prior to the date of transition shall lapse.

(iv) The above principles shall apply to such residential and residential cum commercial properties to which the new tax rate applies.

(v) Credit pertaining to Capital Goods shall be distributed between residential and commercial property on pro-rata basis. Life cycle of capital goods shall be considered 60 months. ITC reversal on capital goods to the extent of the remaining part of life cycle after 01.04.2019 and utilized in projects to which above rate applies shall be done.

2. Issues pertaining to Mixed Immovable Properties:

Concern was raised by States in the meeting that in case of supplies of mixed nature i.e. residential cum commercial properties, commercial construction up to certain percentage of the overall construction should be allowed as such segregation would be a problem for small builders.

Fitment Committee's suggestion:

(i) In mixed properties commercial portion to be allowed upto 15% (on carpet area basis). The commercial property in such mixed properties shall attract GST @ 5% in case of both affordable housing and non affordable housing complex.

(ii) The mixed property which is not eligible for the new tax rate (i.e cases where percentage of commercial property exceeds 15%), shall be taxed as follows:

a) Commercial property shall be taxed at the merit rate as operational now along with ITC facility.

b) Residential property shall be taxed at new rate without ITC.

c) The ITC in relation to the residential property shall not be eligible (to be lapsed as per the design of the new scheme).

d) For the mixed property transition treatment in relation to residential property shall be the same as for the main transition provisions (as per principles detailed at Issue 1 above).

V. Procedure to implement exemption on transfer of development rights, development rights in a joint development agreements (JDA), long term lease (premium), FSI and other similar rights and modalities of calculation for withdrawal of exemption and reversal of ITC credit

GoM recommendations before the GST Council for consideration

- Intermediate tax on development right, such as TDR, JDA, lease (premium), FSI shall be exempted both in its first supply and in its subsequent supplies for residential property only for which no completion certificate is issued at the time of supply.
- Calculation for withdrawal of exemption and reversal of ITC credit to be worked out by the Fitment Committee for flats which are sold after issuance of completion certificate as no GST is payable on them.
- Issues raised by CCT, Maharashtra relating to real estate sectors would be discussed in the joint meeting of Law Committee and Fitment Committee, to be placed before the GST Council.

Issues raised by States:

1. Issue: Regarding withdrawal of tax exemption on TDR etc. in respect of completed properties

- Valuation of the property unsold at the time of issuance of completion certificate is difficult to ascertain and becomes further complex, if it is put to self use.
- Value of property sold from time to time will change even though the inputs used are largely same, hence reversal may be adversely affected.
- Under construction commercial properties attract standard GST rate with ITC, this will result in huge evasion by booking credits against projects that are taxable
- To tax premiums on such long term leasing @18% for completed properties may result in a situation where GST on such rights itself may be higher than 5% of the full value of the completed properties.

Fitment Committee's Recommendations:

(i) It is proposed that the withdrawal of exemption on TDR, Long Term lease (premium) etc. attributable to property remaining unsold on completion may be done as per the following formula:

GST payable on TDR, Long term lease (premium), FSI etc. attributable to immovable property for which completion certificate(CC) has been received during the relevant return period **X** *(Total area of residential property unsold on the date of issuance of CC ÷ Total area of the residential property in respect of which CC has been issued during the relevant return period).*

(ii) Liability to pay GST on development rights, long term lease of land (premium), FSI etc. shall be shifted to the date of issuance of completion certificate under section 148, so that the interest liability starts after issuance of completion certificate and not from the time of supply.

(iii) Liability to pay GST on TDR etc may be placed on the recipient under RCM.

(iv) Further the withdrawal may be limited to 5% (1% in case of affordable) of value of unsold property.

a) On unsold residential property (unsold at the time of issuance of completion certificate): GST to be levied on transfer of development rights (TDR), long term lease of land (premium) or FSI at merit rate and the tax payable shall not exceed 5% (1% for affordable) of the gross value of unsold residential property.

b) Unsold commercial property (unsold at the time of issuance of completion certificate) : GST to be levied on transfer of development rights (TDR), long term lease of land (premium) or FSI at merit rate and shall not exceed 5% of the gross value of unsold commercial property.

(v) Value of unsold property may be deemed to be the value of the property sold nearest to completion.

(vi) Value of supply of service by way of transfer of development rights or FSI by a person to the builder/developer against consideration in the form of constructed dwelling or commercial units shall be deemed to be equal to the value of similar dwelling or commercial units charged by the builder/developer from the independent buyers nearest to the date on which such development rights or FSI is transferred to the builder/developer.

Fitment Committee Comments:

Regarding the issue of withdrawal of exemption of tax exemption on TDR, long term lease (premium) etc, concern has been raised to ensured that the tax liability arising due to withdrawal of exemption on account of unsold property does not exceed 5% (1% for affordable housing) of the value of unsold property. In case where it exceeds, it shall result in a situation where the effective tax paid on the unsold property is more than tax paid on property sold prior to issuance of completion certificate, thereby creating differential tax treatment for the two properties. To address this issue, it has been proposed to cap the tax liability arising out of such withdrawal of exemption to the amount that would have been payable assuming that such property were sold prior to issuance of completion certificate.

2. Issue: Operation of withdrawal of exemption in case of Co-Developer model of JDA

Fitment Committee Recommendation:

(i) In case of unsold property in Co-Developer model (unincorporated Association of Person, i.e of land owner(s) and developer(s)):

a) The liability to pay GST on the supply of construction service shall be upon the co-developers respectively for their respective portions of immovable property sold before completion.

b) The liability for reversal of exemption on TDR in respect of property remaining unsold in the hand of co-developers shall be on the respective co-developers in whose hands the unsold properties remain. In this case the responsibility of not availing ITC on inputs and input services shall rest on the person supplying works contract who is part of the unincorporated AoP.

(ii) In case a partnership is created for such developments the liability of GST as well as TDR(on withdrawal of exemption) shall be on the partnership.

3. Issue: Apportionment of ITC for blockage between different projects, i.e. between commercial and residential projects and between immovable property sold before and after issuance of completion certificate.

Fitment Committee Recommendations:

(i) Apportionment between residential and commercial project: It shall be done on self assessment basis by the developer. The same shall be subject to audit and intelligence based enforcement. Guidelines to apportion the purchases between residential and commercial projects are as under:

- Purchases exclusively for commercial property may be apportioned to commercial projects.
- Purchases exclusively for residential property may be apportioned to residential projects.
- Purchases common to both commercial and residential construction may be apportioned in the ratio of the carpet area of residential and commercial projects under construction.
- 80:20 ratio shall be verified for residential segment at the end of the year and at the end of the project.

(ii) Apportionment between immovable property sold "before Completion certificate" and "after Completion certificate": This shall not be required as ITC will not be available in both the cases**.**

VI. Other issues which were mentioned on 20/2/19.

1. Issue: The date of implementation of the proposed scheme should be 1st April 2019.

Fitment Committee Comment:

The compliance burden shall be reduced if the scheme is implemented from new financial year. Further it shall give time to the industry to make transition to the new tax structure.

2. Issue: Whether the scheme is to be made optional or mandatory?

Fitment Committee Comments:

The scheme may be made optional for the ongoing projects as it shall ease the compliance burden and avoid the ordeal of transition provision compliance.

3. Issue: To keep long term lease and TDR outside the GST for all purposes and leave them exclusively for States until real estate is fully brought in GST. Definition of immovable property under General Clauses Act defines it to include both land as well as the benefits arising out of land

Fitment Committee Comments:

- General clauses Act does not define land. [It defines "immovable property" according to which immovable property shall include land, benefits to arise out of land, and things attached to the earth, or permanently fastened to anything attached to the earth.]
- What has been kept out of GST is supply of land and buildings and not benefits arising out of land.

- Para 2 of Schedule II to the CGST Act states that any lease, tenancy, easement, license to occupy land is a supply of service.
- In the WP 12194/2017 in the case of Builders Association of Navi Mumbai vs Government of India and others, the Hon'ble Bombay High Court has unequivocally held that the demand for payment of GST on the supply of land on lease, the consideration for which is in the form of one time lease premium, is in accordance with the law. The High Court has held as under:
    - *"The substantive provision section 7 in clearest terms says that the activities specified in Schedule I made or agreed to be made without a consideration and the activities to be treated as supply of goods or supply of services referred to in Schedule II would be included in the expression "supply". However, clause (a) of sub-section (1) of section 7 includes all forms of supply of goods or services or both such as sale, transfer, barter, exchange, licence, rental, lease or disposal made or agreed to be made for a consideration by a person in the course or furtherance of business. We referred to the definitions simply to reinforce our conclusion that the CIDCO is a person and in the course or in furtherance of its business, it disposes of lands by leasing them out for a consideration styled as one-time premium. Therefore, if one refers to Schedule II, section 7, then, Item No. 2 styled as land and building and any lease, tenancy, licence to occupy land is a supply of service. Any lease or letting out of a building, including commercial, industrial or residential complex for business, either wholly or partly is a supply of service. It is settled law that such provisions in a taxing statute would have to be read together and harmoniously in order to understand the nature of the levy, the object and purpose of its imposition. No activity of the nature mentioned in the inclusive*

provision can thus be left out of the net of the tax. Once this law, in terms of the substantive provisions and the Schedule, treats the activity as supply of goods or supply of services, particularly in relation to land and building and includes a lease, then, the consideration there for as a premium/one-time premium is a measure on which the tax is levied, assessed and recovered. We cannot then probe into the legislation any further."

- As regard levy of stamp duty on long term lease of land, it is submitted that stamp duty is payable on renting of immovable property for even 1 year or shorter. Stamp duty is also payable on insurance policies and sale of ships and vessels. The fact is that Stamp duty is payable on conveyance document and not on supply and therefore has no relevance in determining taxability of a supply covered under GST.

  Fitment Committee's view: Therefore, there is no legal challenge to levy of GST on supply of development rights or long term lease of land.

4. **Issue**: Deeming fiction of abatement for value of land encroaches upon power of the State to tax Land.

Fitment Committee Comments:

- Supply of construction services is a continuous service, payment of which is made in installments by the buyer. Tax is payable on each installment. To provide abatement of actual value of land in each installment will place huge compliance burden on the developer, particularly because value of land will fluctuate over the period of construction.

- Price at which the developer purchased the land cannot be taken as a basis to value the land or undivided share of land transferred to the buyer of the flat as it may increase by the time it is transferred to the buyer and moreover, builder may charge a higher price.
- In taxation, machinery provisions can be made for approximations.
- Furthermore, if the tax liability is calculated on property by providing actual abatement and subjecting high end property to higher GST rate and treating the same to the effective rate of 5% with deemed abatement, it results into comparable tax incidence.

  Tax = Value x Rate [Value = 100]

  (i) at 33% abatement and 7.5% tax rate;

  Tax = 100 x 7.5% x 67% = Rs 5

  (ii) at 50% abatement and tax rate of 10.5%

  Tax = 100 x 10.5% x 50% = Rs 5.25
- **Fitment Committee's view: Therefore, the issue raised does not impact the proposal to implement the GoM recommendations.**

5. Issue: To bring real estate into GST

Fitment Committee Comments:

It involves larger issue of taxation of land and would require changes in the Act. A committee may be constituted to work out the details.

VII. Other issues which would be examined in due course of time-

1. Cancellation of booking of flats
2. Surrender / relinquishment of tenancy rights.

3. Exemption of long term lease(30 years or more) in all situations, excluding the present exemptions.

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