

In JDAs, capital gains are taxable only if all conditions of s.53A of TOPA fulfilled; developer to demonstrate willingness to perform its obligations under development agreement

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In brief

The Chennai Income-tax Appellate Tribunal (Tribunal), in the taxpayer's case, held that in case of joint development agreements (JDAs), if there was no willingness on the developer's part to perform its obligations under the JDA, it could not be said that development rights were "transferred" within the meaning of section 2(47) of the Income-tax Act, 1961 (Act). Obtaining approval for the building plan was essential to demonstrate willingness on the developer's part to perform its obligations.

In detail

Facts

- The taxpayer¹, a company engaged in the manufacture of cables, entered into a JDA with A Firm on 23 November 2005 to develop a residential project. Under the JDA, in consideration of transferring development rights, the taxpayer was to receive a consideration of 37.54% of the saleable value of the developed property. The JDA was not registered. The taxpayer had received INR 1 Million as a refundable deposit.
- The taxpayer also entered into an Agreement of Sale for the same land with the same developer on the same date.
- The taxpayer offered capital gains arising from the Agreement of Sale on the basis of guideline value for the assessment years (AY) 2008-09 and 2009-10.
- The tax officer (TO) took the view that there was "transfer" of development rights on the JDA date and accordingly taxed capital gains in AY 2006-07.
- The Commissioner of Income-tax Appeals [CIT(A)] upheld the TO's order.

Issue before the Tribunal

Would the capital gains be taxable in AY 2006-07, the year the JDA was entered into?

Taxpayer's contentions

- The taxpayer submitted that capital gains should have been computed by taking into account the Agreement of Sale against the JDA. Hence, capital gains tax incidence should not have been shifted to the first year, i.e., AY 2006-2007.
- The taxpayer relied on the decision of the Punjab and

¹ ITA Nos. 1944 to 1949/Mds/2013
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Haryana (P&H) High Court (HC) in the case of C S Atwal,² wherein it had been held that if the JDA was not registered, the transaction could not be regarded as a “transfer” under section 2(47)(v) of the Act.

- The taxpayer submitted that the treatment of the cost in the developer’s hands should also be taken into account while determining the taxpayer’s taxability. If the cost of the land was recorded by the developer in the subsequent AYs – i.e., AY 2008-09 to AY 2011-12 – then the capital gains tax incidence should not have been shifted to AY 2006-07.

Revenue’s contentions

- The Agreement of Sale did not exhibit characteristics of a true and independently existing sale agreement. The JDA overcame the apparent deficiency in the Agreement of Sale that would stand the test before the Courts, in case of dishonour of terms and conditions. Hence, the JDA was in operation against the Agreement of Sale.
- The taxpayer was liable to pay tax on capital gains based on the consideration he was entitled to receive at the time of transfer, irrespective of the fact that no capital gains accrued on actual receipt of lesser sales price in the subsequent year.
- Reliance was placed on the decisions in T V Sundaram Iyengar & Sons,³ Dr. Maya Shenoy⁴ and Chaturbhuj Dwarkadas Kapadia⁵.

Tribunal’s ruling

- The Tribunal held that in order to invoke section 2(47)(v) of the Act, it needed

to be demonstrated that the conditions of section 53A of the Transfer of Property Act, 1882 (TOPA) were satisfied. One necessary condition of section 53A of TOPA was willingness on the part of the transferee to perform his part of the contract.

- In view of the following facts, the Tribunal held that the developer could not have been said to “be willing to perform his part of the contract”:
 - As per the JDA, the taxpayer had not handed over possession of the property to the developer. Till such possession was handed over, the developer was only licensed to enter the property for the limited purpose of development and construction.
 - The taxpayer received a meagre refundable deposit of INR 1 Million as against the consideration of 37.54% of the sanctionable construction area. Hence, the same could not be construed as receipt of part sale consideration.
 - There was no evidence to show that the developer had obtained approval for the building plan from the municipal corporation before 31 March, 2006 (i.e. during AY 2006-07). Since the building plan sanction was of utmost importance to implementation of the JDA, the very genesis of the Agreement failed in absence of obtaining this sanction.
 - In the absence of approval for the building plan, there was no construction during AY 2006–2007. Hence, the developer incurred no cost

of construction in the AY 2006-07. Thus, during AY 2006-07, the developer had not shown its readiness to execute the JDA.

- The Tribunal held that handing over possession of the property was only one of the conditions of section 53A of the TOPA, but it was not the sole and isolated condition. Further, without accrual of the consideration to the taxpayer, the taxpayer was not expected to pay capital gains on the entire sale consideration.
- Accordingly, the Tribunal held that capital gains could not be taxed during AY 2006-07.

The takeaways

The Tribunal has re-emphasised that to invoke section 2(47)(v) of the Act, all ingredients of section 53A of the TOPA need to be satisfied. However, at what point of time it could be said that the transferee was willing to perform his part of the contract would depend on the facts of the case. Whether actual obtaining of the plan approval or a step taken by the transferee towards obtaining approval can be considered satisfactory can be a subject matter of litigation with the tax authorities.

Let’s talk

For a deeper discussion of how this issue might affect your business, please contact:

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² C S Atwal v. CIT ITA No. 200 of 2013 (O&M) dated 22 July, 2015.

³ T V Sundaram Iyengar & Sons v. CIT [1959] 37 ITR 26 (Madras)

⁴ Dr Maya Shenoy v. ACIT [2009] 124 TTJ 692 (Hyderabad)

⁵ Chaturbhuj Dwarkadas Kapadia v. CIT [2003] 260 ITR 491 (Bombay)

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