
Delhi High Court holds that no service tax can be levied on sale of flats under construction

June 10, 2016

In brief

In 2005, service tax was levied on the construction of residential complexes. In 2010, an explanation was added to the taxing entry, which resulted in sale of flats under construction being deemed to be taxable services. Further, a new taxable service was also introduced in 2010, which levied service tax on any charges collected for providing any preferential location in the complex.

The levy of service tax on sale of under construction flats and on preferential location charges was challenged in Delhi High Court (HC) by way of a writ petition.

In detail

High Court ruling

The HC in its judgment¹ held that while sale of flats under construction involves an element of service, it also involves sale of goods involved in construction and undivided share in the land. The courts, in other rulings, have upheld the levy of service tax on services involved in construction. However, as per the provisions of service tax law, either the law or any rules issued under it should provide for determination of value of taxable services involved in such composite contracts. Presently, there is no provision under the law or under any rules to determine the value of taxable services in such contracts involving sale of land. Grant of abatement by notification cannot overcome

the lack of statutory provisions to ascertain the value of taxable services. In the absence of a statutory mechanism to compute the service tax liability, no service tax can be levied in such cases.

The court further held that amounts collected for preferential location are subject to service tax, since these amounts represent the value of satisfaction derived by a customer from additional attributes of the property and it cannot be traced directly to the value of any goods or land.

The takeaways

While previous rulings had upheld the levy of service tax on sale of flats under construction, this decision has effectively overruled the levy, by holding that no service tax can be levied in the absence of

computation mechanism. This is a decision with considerable ramifications to the industry and the Government is likely to appeal against this decision before the Supreme Court. There is also a possibility that the Government may amend the law to incorporate the computation mechanism to deduct the value of land, as referred to by the court.

Let's talk

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

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¹ TS-231-HC-2016(Delhi)-ST

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