

Real Estate Update

January 29, 2013

VALUE OF FSI AND TDR NOT TO BE INCLUDED IN LAND VALUE UNDER SECTION 50C OF INCOME TAX ACT

Transfers of immovable property are required to take place at a fair valuation as per Indian tax laws. In a judgment that could have significant consequences for the real estate sector, the Mumbai Bench of the Income Tax Appellate Tribunal ('ITAT') has recently ruled, in *Income-tax Officer v. Shri Prem Rattan Gupta*¹, that the Transfer of Development Rights ('TDR') and Floor Space Index ('FSI') cannot be subject of consideration under the fair valuation provisions of section 50 C² of the Income Tax Act, 1961 ('Act'). The ruling was based on the rationale that section 50C refers to 'land and building' and consideration in respect of other capital assets cannot be considered.

BACKGROUND

The Taxpayer, Shri. Prem Rattan Gupta, was the joint owner of property which originally measured approximately 2242 Sq. m. A development agreement was entered into by the co-owners in 2005, with the Public Works Department and the Thane Municipal Corporation ('Acquiring Authorities'), as per which the entire plot was agreed to be sold for development. However, the actual land acquired amounted to 100% Sq. m. for the Eastern Express Highway, 950 Sq. m. for the service road and 300 Sq. m. for the Old Agra Road, being 2110 Sq. m. The co-owners were thus left with 134 Sq. m. (67 Sq.m. belonging to the Taxpayer which was subsequently transferred and which formed the subject matter of this case). The transfer of the 134 Sq.m. was for ₹ 20 lakhs of which the Taxpayer was paid ₹ 10 lakhs.

The assessing officer was of the view that the property should be valued for more since it had development rights attached to it. The matter went up in appeal and the CIT(A) relied on the ITAT decision in *Shakti Insulated Wires (P) Ltd. v. ITO*³ to rule in favour of the taxpayer. He further rejected the computation of the AO on the basis that the stamp value of the entire property as per the development agreement entered into in 2005 was ₹ 1,19,72,064, which prorated would have been ₹ 7,14,910 for 134 Sq.m, which was significantly lower than the payment to the co-owners of ₹ 20 lakhs.

The key issue in this case therefore was the means of valuation of the 134 Sq. m. transferred by the co-owners (of which the taxpayer owned 67 Sq.m), and whether the value of TDR should be included in the fair value of land transferred by the taxpayer.

ITAT'S ORDER

The ITAT observed that, as there had been no reference to the valuation officer ('DVO') as required under section 50C in situations where there is a dispute as to the appropriate value. The ruling of the CIT(A) was therefore set aside and the assessing officer directed to refer the matter appropriately to the DVO. The ITAT further observed that in arriving at a valuation, the DVO should consider the acquisitions already made by the Acquiring Authorities and consider only the net value of land transferred. It was further directed that the DVO should exclude value of FSI and TDR for the purpose of section 50C of the Act as the section uses the expression 'land or building' and not 'immoveable property' which may have a wider connotation.

ANALYSIS

The Explanatory Notes to Circular No. 8 of 2002⁴ ('Circular') provide that Section 50C⁵ was to be a special provision for full value of consideration for transfer of 'immovable property'. The Circular provided that where the sale consideration of 'land or building or both'⁶ was less than the value adopted for the purpose of stamp duty, the value so adopted shall be used for computation of capital gains under the Act⁷. Further, in *Kishori Sharad Gaitonde v. Income Tax The Hon'ble Tribunal*⁸, while analyzing section 50C, the ITAT held that section 50C operated by way of fiction and therefore such provisions should be strictly interpreted. Consequently, only capital assets being land and building and not any capital asset could be considered for section 50C.⁹

Clearly there has been a difference in approach based on whether the term "immovable property" is used, as against the term "land and building" as contemplated in section 50C. Therefore the reasoning adopted by the ITAT in the present case is in corroboration of the position of law and in sync with other judgements of the ITAT under which rights similar to TDR and FSI have been held to not be subject to valuation under section 50C¹⁰. By dismissing the Assessing Officer's presumption that external considerations such as TDR and FSI should be included in the value of property, over and above stamp value applicable to land and building, the ITAT has provided additional clarity that should hopefully prevent unnecessary litigation on valuation issues in real estate deals. It would also remain to be seen if the same benefit is accorded to joint development agreements.

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¹ ITA No. 5803 of 2009 pronounced on 28.03.2012 by ITAT "C" Bench.

² Special provision for full value of consideration in certain cases.

³ ITA 3710/Mum/2007 dated 27.04.2009.

⁴ Circular available at http://law.incometaxindia.gov.in/DIT/File_opener.aspx?page=CIR&schT=&csId=7c1b8cd4-8f29-480f-9aab-9286b1b2f837&cm=8&yr=2002&sch=&title=Taxmann.

⁵ Section 50 C (1) - Where the consideration received or accruing as a result of the transfer by an assessee of a capital asset, being land or building or both, is less than the value adopted or assessed [or assessable] by any authority of a State Government (hereafter in this section referred to as the "stamp valuation authority") for the purpose of payment of stamp duty in respect of such transfer, the value so adopted or assessed 11[or assessable] shall, for the purposes of section 48, be deemed to be the full value of the consideration received or accruing as a result of such transfer. Section 50C was inserted with effect from April 1, 2003.

⁶ Clause 37.2 of the Circular, supra note 4 above.

⁷ This intention was also reflected in the Finance Act, 2002.

⁸ ITA No. 1561 of 9 of 2009, Mumbai Branch, ITAT.

⁹ In this case, ITAT held that 'tenancy rights' even though a capital asset, was not covered by section 50C of the Act.

¹⁰ Supra note 8. See also Iqbal Abdul Kader Fazlani v. ACIT ITA No. 8831 of 2011 and ITA No. 8832 of 2012 where shares in immovable property was sought to be valued under section 50C of the Act.

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