L&S UPDATE

An e-update to clients from Lakshmikumaran & Sridharan

12 MAY 2022

INDIRECT TAX

Construction services – Deduction of 1/3rd value towards land is optional: Gujarat HC

UPDATE NO. 20 OF 2022

Lakshmikumaran & Sridharan attorneys

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BRIEF FACTS

a) The lead petitioner entered into an agreement with developer for the purchase of a plot of land along with construction of bungalow on the said plot of land. Separate and distinct consideration was agreed upon for sale of land and construction of a bungalow on the land. The construction portion was only about 15-20% of the total agreement value.

b) Other petitioners were developers who have sold / intended to sell developed parcels of land. They filed advance ruling application on the question whether GST is applicable on supply of developed land. The authority held that the deduction for sale of land was admissible only to the extent of 1/3rd of the total consideration.

c) The question before the court was whether paragraph no. 2 of Notification No. 11/2017-Central Tax (Rate) is *ultra-vires* Section 7(2) of the CGST Act read with Entry No. 5 of Schedule III to the Central Goods and Services Tax Act, 2017 as well as *ultra-vires* Section 9(1) and Section 15 thereof.

DECISION OF THE GUJARAT HIGH COURT

1. Paragraph 2 of the Notification No. 11/2017-CT (R) and the parallel State tax Notification which provide for a mandatory fixed rate of deduction of 1/3rd of total consideration towards the value of land is *ultra-vires* the provisions as well as the scheme of the GST Acts. The same is also discriminatory, arbitrary and violative of Article 14 of the Constitution of India.

2. The mandatory deduction of 1/3rd for value of land is not sustainable in cases where the value of land is clearly ascertainable or where the value of construction service can be derived with the aid of valuation rules. However, such deduction can be permitted at the option of a taxable person particularly in cases where the value of land or undivided share of land is not ascertainable.

3. Paragraph 2 of Notification No. 11/2017- CT (R) and the parallel State tax Notification were read down to the effect that the deeming fiction of 1/3rd will not be mandatory in nature. It will only be available at the option of the taxable person in cases where the actual value of land or undivided share in land is not ascertainable.

4. The petitioner had deposited the amount of tax charged by the supplier under protest, consequently the concerned GST authority was directed to refund the excess amount of tax. Refund was directed to be granted along with the statutory interest at the rate of 6% p.a. which is to be calculated from the date of excess payment of tax till the date of refund.

5. The Court also observed that 'sale of land' under Schedule III covers sale of developed land and there is no intention to impose tax on supply of land in any form. However, if development on land is undertaken at the behest of another person, there could be imposition of tax under the CGST Act on the goods and services used in the course of development.

L&S Comments:

- The department is likely to appeal the above decision before the Supreme Court.

  Project wise analysis may be carried out to compare actual value of land and prescribed 1/3rd deduction. Basis the same, taxpayers may declare the tax to be paid as under protest payment and may decide to avail the benefit in case of favorable decision by the Supreme Court.

- The cases where the tax has already been paid claiming 1/3rd deduction wherein the actual value of land was more and ascertainable. The possibility for filing refund claims may be explored.

  Proper clauses in Builder Buyer Agreement and other documents to be ensured to claim actual value of land as a deduction from the total consideration.

- Plot Sale Agreements need to be reexamined in the light of the observation of the Court on the taxability of development activities undertaken at the behest of the potential plot buyer.

[*Munjaal Manishbhai Bhatt* v. *Union of India* – Judgement dated 6 May 2022 in R/Special Civil Application No. 1350 of 2021 and Ors., Gujarat High Court]

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