

TAX FLASH NEWS

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Deduction of 1/3rd of total consideration towards the value of land is ultra-vires – Gujarat High Court

Executive Summary

Hon'ble Gujarat High Court has held that 1/3rd deduction from total consideration towards the value of land is ultra-vires the provisions as well as the scheme of the GST Act. It has further held that such deduction is optional in cases where the value of land is clearly ascertainable or in cases where the value of construction service can be derived through the aid of existing valuation rules.¹

Facts of the case

- 'Petitioner' entered into an agreement with a 'Developer' for purchase of a plot of land and construction of bungalow on the said plot.
- Separate and distinct consideration was agreed upon between parties to the agreement for sale of land and construction of bungalow.
- As per the agreement, Petitioner was liable to pay all taxes including GST. Petitioner believed that GST would be payable on consideration payable for construction of bungalow in as much as it would constitute supply of construction service.
- Relying upon entry no. 3(if) of Notification No. 11/2017-Central Tax (Rate) dated 28 June 2017 read with paragraph 2 of the said notification, Developer informed the Petitioner that 9% CGST plus 9% SGST would be payable on the entire consideration payable for land as well as construction of bungalow after deducting 1/3rd of the value towards the land.
- In the above circumstances, Petitioner filed writ application.

Petitioner's contentions

- It is a settled legal position that a delegated legislation cannot travel beyond the scope of the parent legislation.

- By virtue of section 7(2) of the GST Act, transactions specified in the Schedule III are excluded from purview of supply. Sale of land is included in the entry no. 5 of the Schedule III to the GST Act. Imposition of tax on consideration received towards the sale of land by virtue of delegated legislation (i.e. by notification) is ultra-vires sections 7 and 9 of the GST Act.
- As per the minutes of 14th GST Council meeting, the abatement of 1/3rd value towards the land was thought of only in respect of sale of flats/apartments and not in respect of the transactions where land was sold separately.
- Detailed valuation mechanism is available in the statute which is primarily based on actual consideration and such provisions cannot be ignored by simply providing adhoc and arbitrary abatement for land by way of a notification.
- Section 15(5) provides that the value of deemed supplies shall be determined in such manner as may be "prescribed". The term "Prescribed" as per section 2(87) means prescribed by rules.

Revenue's contentions

- Section 15(5) (ambit under which impugned notification is notified) provides that notwithstanding anything contained in subsection (1) or sub-section (4), the value of such supplies as may be notified by the Government on the recommendations of the Council shall be determined in such manner as may be prescribed.
- Impugned notifications have been issued in the pursuance of the recommendation of the GST Council. Therefore, question of impugned entry in the notification being ultra vires section 7(2), section 9(1), section 15 of the CGST Act 2017 and Article 14 and 246A of the Constitution of India does not arise at all.

¹ Munjaal Manishbhai Bhatt vs Union of India [2022-VIL-319-GUJ]

- In the 34th GST Council meeting, the Council agreed to apply tax at new rates. Consequently, Notification No. 03/2019-Central Tax (Rate) dated 29 March 2019 (amending impugned notification) was issued. It provided for deemed valuation of the land as provided in paragraph 2 of the notification.
- Concerned transaction is for sale of a developed piece of land and not of a plain land as it is subjected to many conditions, limitations, prohibitions and restrictions unlike a transaction of sale of land. Therefore, transaction does not fall under Schedule III but under entry 5(b) of Schedule II.
- Consideration as provided in the booking agreement with respect to the land and construction are decided inter se the parties and the same might not reflect the actual value of the land involved.

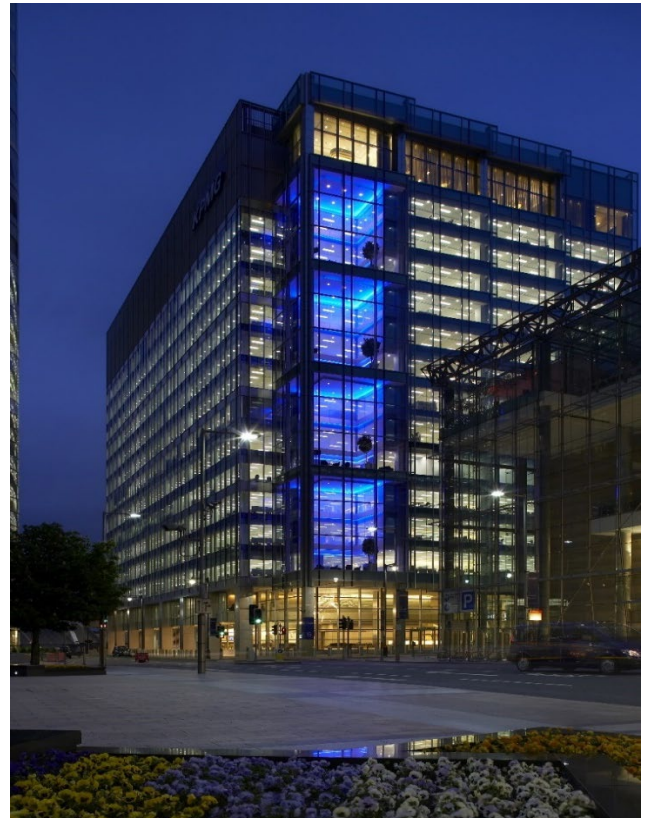
High Court's decision

Hon'ble High Court of Gujarat held that mandatory application of deeming fiction of 1/3rd of total agreement value towards land even though the actual value of land is ascertainable is clearly contrary to the provisions and scheme of the GST Act and therefore ultra-vires the statutory provisions. Below is the gist of the important inferences pronounced by the Court:

- Legislative intent is to impose tax on construction activity. There is no intention to impose tax on supply of land in any form and it is for this reason that it is provided in the Schedule III to the GST Act that the supply of land will be neither supply of goods nor supply of services.
- "Sale of land" under Schedule III to the GST Act covers sale of developed land.
- When the statutory provision requires valuation in accordance with the actual price paid and payable for the service and where such actual price is available, then tax has to be imposed on such actual value. Deeming fiction can be applied only where actual value is not ascertainable.
- On perusal of 14th GST Council meeting minutes, it becomes clear that the deduction was contemplated only in the context of flats wherein it was difficult to ascertain the value of the undivided share of land.
- Prescription under section 15(5) of the GST Act has to be by rules and not by notification.
- Impugned paragraph 2 of Notification (supra) is 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.

Our comments

The real estate sector has always been requesting for different abatement based on geographic region since value of land, at times, determine the value of flat. Hence, applying standard deduction towards land across India creates divergency. This judgment can have big impact for the real estate sector, specifically where there is practice of having separate agreements for sale of land and construction. We will have to wait on the next steps by Government as to whether they challenge the same or any amendment is brought in the valuation rules.



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