

**BUILDERS UNDER SERVICE TAX NET FOR  
SALE OF FLATS**



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The life of builder had become more complicated after explanation inserted under finance act for taxable service under section (105) (zzq) commercial or industrial construction service and under section (105) (zzzh) construction of complex service. After facing recession time in previous year, now new deeming provision of Service tax is to be also faced by the builders. It is necessary to know silent features of inserting the deeming provision inserted in the finance act. Therefore it is better to understand the basics of inserting this new provision under finance act:-

**Silent feature of Implementation of Service Tax on Builders on Sale of Flat:-**

It has been explained in explanation issued on 26.02.2010 vide D.O.F. No.334/1/2010-TRU that the builders usually sign an agreement with buyer named "Agreement to Sale" and reserve a flat for buyer before commencement/completion of construction and receive consideration in installments from buyers. In said case builders grant possession of the property when the entire consideration is being paid and the construction is over. In some other cases in initial stage, instruments are created between the promoter and all the buyers (which may include a person who has provided the vacant land for the construction), known as 'Sale of Undivided Portion of The Land'. This instrument transfers the property right to the buyers though it does not demarcate a part of land, which can be associated with a particular buyer. Since the vacant land has lower value, this system of legal instrumentation has been devised to pay lesser stamp duty. In many cases, an instrument called 'Construction Agreement' is parallelly executed under which the obligations of the promoter to get property constructed and that of the buyer to pay the required consideration are incorporated.

These different patterns of execution, terms of payment and legal formalities have given rise to confusion, disputes and discrimination in terms of service tax payment. In order to achieve the legislative intent and bring in parity in tax treatment, an Explanation is being inserted to provide that unless the entire payment for the property is paid by the prospective buyer or on his behalf after the completion of construction (including its certification by the local authorities), the activity of construction would be deemed to be a taxable

service provided by the builder/promoter/developer to the prospective buyer and the service tax would be charged accordingly. This would only expand the scope of the existing service, which otherwise remain unchanged. Thus, in order to achieve the legislative intent of collecting more revenue, the changes have been carried out with a clear intention of expanding the scope of existing services.

#### Explanation Inserted by the finance act

The case of commercial construction section 65(105) (zzq) and *construction of complex (105) (zzzh)* Explanation has been inserted to cover the scope of service provided by builder under tax net, the relevant section with explanation is being reproduced as follow:

*(105) (zzq) "Taxable service" means any service provided or to be provided to any person, by any other person, in relation to commercial or industrial construction*

*"Explanation.—For the purposes of this sub-clause, the construction of a new building which is intended for sale, wholly or partly, by a builder or any person authorised by the builder before, during or after construction (except in cases for which no sum is received from or on behalf of the prospective buyer by the builder or the person authorised by the builder before grant of completion certificate by the authority competent to issue such certificate under any law for the time being in force) shall be deemed to be service provided by the builder to the buyer;"*

*(105) (zzzh) "Taxable service" means any service provided or to be provided to any person, by any other person, in relation to construction of complex,*

*"Explanation.—For the purposes of this sub-clause, construction of a complex which is intended for sale, wholly or partly, by a builder or any person authorised by the builder before, during or after construction (except in cases for which no sum is received from or on behalf of the prospective buyer by the builder or a person authorised by the builder before the grant of completion certificate by the authority competent to issue such certificate under any law for the time being in force) shall be deemed to be service provided by the builder to the buyer;"*

Explanations inserted in finance act to cover builders within the tax-net through "deeming" provisions". addition of "*Explanation*" in clause 105(zzzh) and (zzq) extend the scope of the services relating to commercial and industrial construction and complexes by treating the amount received by the builder as services rendered for the Construction of flat on behalf of buyers. Addition of said explanations in clause 105(zzzh) and (zzq) is effective from 01.07.2010 under service tax.

## Impact & Scope of Explanation

The Impact of implementation of said explanation is that in cases where builder are taking advances from prospective buyers by signing an agreement and receiving balance amount in installments, then it will be liability of builders to pay service tax on amount received in advance or installments.

In cases where builders are constructing flats from his own amount and selling the flats on after getting completion Certificate from approved authorities to the buyers are still exempted for Service tax. Now its time to analyze impact of tax liability apply in the following cases :-

| <b>CASES TO BE ANALYZE</b>   | <b>RERULTS</b>   |
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| <b>First Case: - In a Case where the date of execution of contract is before 01.07.2010 and Completion Certificate is received from approved authority before 01.07.2010. On other hand full payment is received also before 01.07.2010.</b> | <b>Result: - Said case is excluded from service tax net as Completion Certificate has already been issued before 01.07.2010. Therefore no Liability of payment of Service tax in said case.</b>  |
| <b>Second Case: In a Case where the date of execution of contract is before 01.07.2010 and Completion Certificate is received from approved authority before 01.07.2010. But the payment is received after 01.07.2010.</b>                   | <b>Result: - Said case is also excluded from service tax net as Completion Certificate has already been issued before 01.07.2010. Although the payment is received after 01.07.2010. As the service provided before implementation of explanation due to receipt of Completion Certificate before 01.07.2010. Therefore no Liability of payment of Service tax in said case.</b> |
| <b>Third Case:- In a Case where the date of execution of contract and payment is before 01.07.2010 but Completion Certificate is received from approved authority after 01.07.2010.</b>  | <b>Result: - In this case, no payments are taking place after 30-6-2010 and, hence, the question of tax liability should not arise. However, since the completion certificate has not been received, therefore any amount received by the builder will make it subject to payment of Service tax.</b>  |
| <b>Forth Case: In a Case where the date of execution of contract and</b>   | <b>Result: - In this case since the completion certificate has been</b>  |

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|---|---|
| some payment is before 01.07.2010 and some payment after 01.07.2010 but Completion Certificate is received after 01.07.2010 from approved authority.  | issued after 01.07.2010, question of payment of tax on the payments received from buyer on and after 01.07.2010, till the date of issue of completion certificate will be subject to tax.   |
| <b>Fifth Case:</b> - In a Case where the date of execution of contract and payment is received before 01.07.2010 but Completion Certificate is received before 01.07.2010 from approved authority.                    | <b>Result:</b> - In this case since the completion certificate has been issued before 01.07.2010 and payments has been received before issue of completion certificate, the question of Service Tax does not arise.   |
| <b>Sixth Case:</b> - In a Case where the date of execution of contract is after 01.07.2010 and payment is received before 01.07.2010 but Completion Certificate is received after 01.07.2010 from approved authority. | <b>Result:</b> - In this case since the completion certificate has been issued after 01.07.2010 but all payments are received before 01.07.2010 therefore as there is no payment balance after 01.07.2010, therefore question of levy of tax does not arise in said case. |

It may be noted that, entering into the contract between the buyer and the builder is of no consequence. Only two things are most important for determining Service tax liability i.e. date of payment received by builder and date of issuance of Completion certificate from the approved authority.

#### **Valuation of Abatement and Tax on Taxable Amount**

That abatement on deeming sale provision vide notification no. 29/2010 dt. 27<sup>th</sup> June, 2010 which has been incorporated two additional clauses viz. 7(a) and 10(a) in the Notification No. 1/2006-ST dt. 1-3-2006. the essential condition for claiming abatement under both the notification is that the abatement will not applicable in the cases wherein only completion and finishing services have been provided. Secondly and essential thing is, if the Service Provider has collected value of land separately then, provisions in this respect of said clause of notification dated 29/2010 will not be applicable. Which means it is mandatory to add land cost in cost of construction for claiming abatement under said notification.

If the builder had added the cost of land in the construction of flat for sale then abatement @ 75.00% of the gross value of a flat will be applicable to him. The clause 7 provides for abatement in value @ 67.00% while clause 7(a)

**provides for @ 75.00%. Secondly, clause 7(a) is applicable in the cases wherein value of land is part of the value of services rendered. This condition has been provided for negatively. It means that inclusion of value of land in the total value of service is not required to be proved. As long as the Service Provider is not recovering value of land separately abatement @75.00% will be applicable. If a builder does to violation of the condition laid down under clause 7(a). Such cases will be covered by the clause 7. This will be make builder unhappy by converting abatement of notification no. 1/2006 from 75% to 67%.Tax liability arising on account of reduction in abatement value will have to be paid with interest by the builders for not fulfilling the conditions.**

**The builder are like a ship floating in the sea, who had not properly recovered from tsunami of recession, now a new tides of the service tax had trapped them by imposition of service tax liability on sale of flat through “deeming provision” by central government in this financial budget. Now builders have to be more careful and prompt for compliance of provisions related to Service tax in their regular routine from 1<sup>st</sup> July 2010.**