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# Guidance on tax deduction from the consideration payable for transfer of immovable property

**Executive Summary** **6 June 2013**

By the Finance Act 2013, Income Tax Act has been amended to introduce section 194-IA which mandates deduction of tax at source by any person who is a transferee of an immovable property in a case where the transferor is a person resident of India and the consideration for the transfer is INR 50 lakhs or more. The tax is required to be deducted @ 1% of the consideration for transfer. The section has become effective from 1 June, 2013. The rules for payment of the tax and issuance of certificate to the deductee have been prescribed. It is not mandatory for the tax deductor to obtain TAN.

The provision has far reaching impact on the transactions in real estate, whether, residential, commercial, under construction or ready for sale units. Higher tax deduction @ 20% of the consideration shall apply in case the seller does not furnish PAN. A transaction with builder/developer is also within the purview of the section, though, the Finance Bill 2013 explained the rationale for introduction of the provision as preventing tax evasion in the property deals where the property is sold by the persons who are not registered as tax payers. Generally, builder/developer report the income of a project on completion, while the tax deduction will be effected during the construction phase, resulting into funds blocked during such period, as the tax credit will be linked with and allowed in the year of reporting of the income.

The attached guidance discusses the scope of the provision and some of the complex issues which may arise in practice.

## Salient features of Section 194-IA of the Act

- The tax withholding under the section is attracted when any immovable property is transferred by a resident transferor to any transferee, whether he is resident or non resident. Thus, even a non-resident will have to withhold tax under the provision of the section if he acquires immovable property from a person resident in India
- The transferee may be a corporate entity or a non corporate person such as individual, HUF, partnership firm, etc.
- The immovable property may be residential or commercial. Further, the property may be held by the transferor or acquired by the transferee, as a capital asset or stock-in-trade
- The section shall not apply where the actual consideration for transfer of the property is less than INR 50 lakhs; the value of the property adopted for the stamp duty purpose (whether upward or downward) will not impact the above threshold of INR 50 lakhs
- Tax is required to be withheld at the time of:
  - credit of the consideration to the account of the transferor, or
  - at the time of payment of such sum

  whichever is earlier
- It is not necessary for the transferee to obtain tax deduction account number
- However, if the transferor does not hold or fails to furnish Permanent Account Number, the transferee shall withhold tax @ 20%, instead of the prescribed rate of 1%
- There is no provision or facility for the transferor to apply for certificate for nil or lower tax withholding in a case where he is entitled to full or partial exemption from the tax liability arising from transfer of the property or he is otherwise not liable to tax

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## Issues on the scope of tax withholding under section 194-IA of the Act and PHD's view

1. Definition of immovable property refers to land or building or part of building. Whether transfer of a residential flat, commercial unit, shop, etc. which is not building as such, is within the scope of the section?

   *Yes. In our view, the word "part of building" has been consciously inserted in the definition to include them within the scope of the section.*

2. Whether tax withholding is attracted in the case of transfer of leasehold interest in any immovable property?

   *The immovable property, as defined under the section does not include any right or interest in the property de hors the property. The legislature, where thought fit, has extended the meaning of immovable property by an extensive definition. For example, for the purpose*

*of section 269A(e) immovable property has been defined to specifically include any rights therein. Hence, in our view, transfer of leasehold rights, de hors the property, per se, cannot not be regarded as transfer of the land or building so as to attract the tax withholding. For example, transfer of leasehold interest by the lessor of the property under a sub-lease would not attract the provisions of the section.*

*However, it has been judicially held[1] that a property comprises of a bundle of rights and it is possible to transfer certain rights in the property while other rights retained with the transferor. Hence, in our opinion in principle, a transaction of granting a lease of immovable property, by the owner of the property, for a consideration, may attract tax withholding. The consideration may be in the form of lease premium and/ or lease rent at periodical interval. The threshold of INR 50 lakhs will have to be reckoned with reference to the aggregate amount of the premium and lease rentals payable. However, when the lease rent amount is also subject to tax withholding under section 194- I of the Act, the tax deduction may be restricted to the amount of lease premium only.*

3. Is tax withholding applicable to transfer of the property held by the transferor as "capital asset" or as "stock-in-trade"?

*The scope of the section extends to the property whether held by a transferor as capital asset or stock-in-trade. Similarly, the purpose for which the transferee may acquire the property is of no significance.*

4. What is the meaning of 'transfer' for the purpose of this section?

*Transfer is not defined under section 194-IA. The wider definition of transfer under section 2(47) of the Act, applies only in relation to a capital asset. As mentioned above, the scope of the section is not restricted to capital asset alone. Also, the definition under the aforesaid section 2(47), may be, to some extent, inconsistent with the scope of definition of immovable property under section 194-IA of the Act. In our view, the 'transfer' for the purposes of the section should be understood in the context of The Transfer of Property Act, 1882*

5. Whether, a person who enters into agreement with a builder/developer in accordance with the governing regulations in the state, [for example, under Maharashtra Ownership Flats Act, 1963 (MOFA) in the state of Maharashtra], is liable to withhold tax under the provisions of section 194-IA of the Act?

*The section is applicable where any consideration of INR 50 lakhs and above is payable/paid for transfer of the immovable properties (the specified properties). Hence, in a case where a builder or developer, under an agreement, undertakes to construct a building and to effect conveyance thereof along with land, to a co-operative society formed in accordance with the applicable regulations, a doubt may arise whether it*

[1] A. R. Krishnamurthy (176 ITR 417) (SC)

*is a transaction for transfer of the specified properties by the builder/developer to the flat[2] owner, who, by very nature of the transaction, can obtain only occupancy rights of the flat – the legal ownership vested with the co-operative society. In our opinion, a plausible view would be: that such flat is covered by tax withholding obligation under the said section since the agreement with the builder/developer, apart from the possession of the flat, also contemplates transfer of undivided right, title and interest in the specified property through the membership of a co-operative society and the consideration is paid by the flat buyer for transfer of the said right, title and interest, albeit, undivided i.e. in common with other members of the co-operative society. We must also clarify that the above view will apply, perhaps with greater force, in an Apartment Ownership Model, where a member of a condominium directly acquires specific right, title and interest in the specified property.*

6. In a case where a builder/developer accepts flat booking by an investor, who may, at his option, enter into agreement for purchase of the flat at a later stage; is tax withholding required by the investor at the booking stage?

*In the case of a booking of a flat that tantamounts to an option taken by an investor, the amount paid at that stage, need not be considered as consideration paid by him for transfer of the flat. The better view is that the sum is paid by him by way of an option to retain the right to purchase the specified property at a future date. As and when he exercises the option by entering into purchase agreement, the tax withholding obligation would arise. However, we must hasten to add that payments made by him pursuant to the flat booking will be appropriated by the builder/developer towards the consideration payable against the agreement, hence, the tax withholding at that stage should be complied with reference to whole of the amount so appropriated and further payments made pursuant to the agreement.*

*We may, however, add a word of caution that the above position in law should apply only to the genuine transaction of an option money paid by an investor; any deliberate act or a device for deferment of tax withholding will not be protected from adverse consequences of delayed tax withholding.*

7. Whether tax withholding obligation would arise in the case of resale of a flat by a member, of a co-operative society or, of a condominium?

*As discussed above, when a transferor is a member of a co-operative society who holds occupancy rights of the flat and undivided common right, title and interest in the specified property, the transaction can be said to be a transfer of the specified property that will attract tax withholding obligation*

[2] Flat means a residential flat, commercial office , shop or a gala

8. In the case of an agreement executed between builder/developer for total consideration of, say, INR 100 lakhs of which, INR 25 lakhs is paid upfront and the balance is paid in 5 instalments of INR 15 lakhs each, is tax withholding required at the time of agreement on the entire consideration?

*The section mandates deduction @ 1% of the amount of consideration for transfer of the property, at the time of credit of the amount to the account of the transferor or at the time of payment, whichever is earlier. In our view, the issue needs to be examined under different scenarios, depending upon whether or not transferee maintains books of account, the method of his crediting the consideration to the account of the transferor and timing of payment of the consideration.*

***Scenario I: Transferee maintains books of account***

*In this scenario, assuming that the transferee, as per method of accounting followed by him, credits the account of the builder/developer for INR 100 lakhs at the time of agreement, then he should deduct INR 1 lakh at that stage. However, as per his method of accounting, if INR 25 lakhs is credited to the account of the builder/developer, the tax withholding would be INR 25000 only.*

***Scenario II: Transferee does not maintain books of account***

*In this scenario, the tax withholding obligation would arise at the time, and to the extent, of payment made by way of consideration for the transfer. Accordingly, in the instant case, the tax withholding would be INR 25000 at the time agreement execution and INR 15000 each time when the instalment of INR 15 lakhs would be paid, thus the aggregate tax withholding would be INR 1 lakhs over a period of time.*

9. What would be the tax withholding amount in the above example, in a case, where the agreement is made before 1 June 2013 and installments are paid after the said date?

*If the transferee is maintaining the books of account and has credited entire consideration of INR 100 lakhs to the account of the builder/ developer, then there would be no tax withholding obligation with reference to the transaction. However, in a case where books of account are not maintained or, having maintained the books of account, only INR 25 lakhs has been to the account of the builder/ developer, he will have to deduct tax on the balance amount of INR 75 lakhs, from time to time, after 1 June 2013.*

*Another plausible view that the section should apply only to the agreements made on or after 1 June 2013, appears to be too liberal to be acceptable.*

10. In the above example, out of total consideration of 100 lakhs, if INR 60 lakhs has been paid before 1 June 2013, and thus only INR 40 lakhs is payable after the aforesaid date; whether tax withholding will apply in such case?

*The threshold of INR 50 lakhs is to be reckoned with reference to aggregate consideration paid or payable for transfer of the specified properties. However, payment already made prior to 1 June 2013 cannot be subjected to tax withholding. Hence, in principle, the section will apply in the above situation, however, only the payments made on or after 1 June 2013 shall be liable to tax withholding. Accordingly, in the instant case, tax withholding would be @ 1% of INR 40 lakhs i.e INR 40000 only.*

11. How the threshold of INR 50 lakhs should be applied in a case where the transferor or the transferee is co-owner of the specified property?

*The threshold INR 50 lakhs should be applied with reference to the share of individual co-owner. Thus, if the aggregate consideration for transfer of the specified property exceed INR 50 lakhs but the share of each individual co-owner is less than the above sum, the provision shall not apply.*

12. How the threshold of INR 50 lakhs should be applied in a case where the specified property, is held by the transferor, or to be held by the transferee, as the case may be, jointly with a relative who is party to the agreement only out of the sentiments i.e. without actual beneficial interest in the property?

*In a case where a person being a relative whose name is included in the property document only out of the sentiments without vesting of beneficial ownership, the threshold should be computed with reference to the consideration accruing to the transferor or payable by transferee, as the case may be, who is the actual beneficial owner of the property.*

13. Land is owned by 'A' who has entered into development agreement with developer 'B', pursuant to which, 'A' is entitled to 40% of the constructed area without any cost. 'B' is entitled to sell the balance 60% constructed area to outsiders. No cash consideration is provided by 'B', however, refundable interest free security deposit of INR 10 crores is provided by 'B' to 'A'. The market value of the land put into the possession of 'B' pursuant to the development agreement is INR 100 crores.

In the above factual matrix, is 'A' under an obligation to withhold tax in respect of value of 40% constructed area agreed to be given by 'B' free of cost?

Similarly, is 'B' under obligation to withhold tax in respect of 60% of the land interest transferred by the land owner 'A'?

*The issue, in essence, is, whether the section mandates tax withholding in respect of consideration paid in kind for transfer of the specified property. The section refers to tax withholding with*

*reference to 'any sum paid by way of consideration for transfer……'. The word 'sum', in its natural connotation denotes quantification of a value. In the Act, it has been used at several places, interchangeably with the word 'amount' which also quantifies the value. Hence, 'sum' accompanied with the word 'consideration' may be understood as indicating monetary as well as non monetary consideration. We are fortified in our view on a reference to the provisions of sub-clause (a) of clause (vii) of sub section (2) of section 56 of the Act where the legislative intent of restricting the scope of the section, only to the monetary consideration, is manifest by use of the phrase 'sum of money'. In our view, tax withholding in the case of transfer of the specified property for a non monetary consideration is as much within the scope as the transfer for monetary consideration. The fact that transaction in the instant case is an exchange of asset, is not relevant, because the word 'transfer' has been judicially held[3] as a word of the widest import, the exchange of an asset in common parlance as well as under the Transfer of Property Act, 1882 has been considered within the scope of the transfer. Having said this, we do appreciate that there would be practical challenges in complying with the tax withholding in the instant case. Before dwelling upon it further, we must clarify that, both, 'A' and 'B' will have to comply with the tax withholding in respect of the respective specified property exchanged by them. It may be noted that in a transaction of an exchange, two distinct assets are transferred between the parties. In the instant case, 'A' would acquire 40% of the constructed area in exchange for 60% interest in the land to be transferred in favour of 'B' and vice versa from the perspective of 'B' as a transferor of the specified property. For quantification of tax withholding amount by the respective parties the valuation of the equivalent monetary consideration will have to be ascertained, applying the principles of valuation.*

*The refundable interest free security deposit cannot be construed as a consideration for transfer of the specified properties, hence, it shall not be liable to tax withholding compliance.*

14. Whether tax withholding is attracted in the case of transfer of the specified asset by a wholly owned subsidiary to the parent company or vice versa?

*As discussed earlier, the tax withholding is attracted where the specified property is transferred for a consideration of INR 50 lakhs and above. It has also been discussed that the definition of transfer applicable for computation of capital gains will not apply and that the 'transfer' will have to be understood in the commercial parlance and in the context of the Transfer of Property Act, 1882. No doubt, as per the provision of section 47(iv) and (v) of the Act, for the purpose of computation of capital gains, transfer of property between a parent company*

[3] Mangalore Electric Supply Co. Ltd (113 ITR 655) (SC)

*and wholly owned subsidiary is deemed to be a transaction which is not to be regarded as transfer, but, the same cannot be imported for the purpose of section 194-IA which operates in the field of tax withholding, is applicable, regardless of, the specified asset being capital asset or not. A company, even in a case where wholly owned by parent, continues to have a status independent of its shareholder – the parent company in the instant case. Therefore, notwithstanding the doctrine of substance over form, legally, the parent and the subsidiary company assume the status of being independent entities[4] and can be regarded as a transferor who is distinct from a transferee, and capable of effecting transfer of the specified property and the transfer of property would attract tax withholding where the conditions of the section are satisfied.*

[4] Bacha F Guzdar (27 ITR 1) (SC)
Vodafone International Holding B.V.( 341 ITR 1) (SC)

## Procedural aspects

The Central Board of Direct Taxes (CBDT) has notified rules governing the procedural aspects by notification dated 31 May 2013. The relevant points are stated hereunder.

- The tax withheld by the transferee shall be deposited with the Central Government within 7 days from the end of the month in which the deduction is made. Thus, tax withheld, say, on any day in June 2013 will have to be deposited on or before 7th July, 2013
- The payment shall be made in challan-cum-statement in Form no. 26QB. The salient features of the information required to be submitted in the challan-cum-statement are as follows:
  - Name, address and PAN of the transferee and transferor
  - Whether there are more than one transferor/transferee
  - Date of agreement/booking
  - Total value of consideration
  - Whether the payment of consideration is in instalment or lump sum
  - Date of payment/credit of the consideration
  - Date of deduction and amount of tax
  - Date of deposit and mode of payment
  - A tax deductor being a company or any other person whose accounts are required to be audited under section 44AB of the Act, is required to make the payment by electronic mode
- The transferee is required to issue certificate of payment of tax to the transferor within 15 days from the due date of furnishing the challan-cum-statement. Thus, in example referred to above, certificate will have to be issued by 23rd July, 2013 The certificate in Form no. 16B is required to be generated and downloaded from the notified web portal

## Higher withholding tax rate of 20% if transferor fails to furnish PAN

In a case *where* transferor fails to furnish PAN, the transferee shall deduct tax @20% of the consideration for transfer of the specified properties

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