

## Realty cries foul on service tax

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The provisions in the Budget for 2010-11 levying service tax on renting of commercial property and on residential sales transactions during the project construction phase hold major implications for developers and end-users.

Developers have strongly objected to the service tax provisions which will hike costs at a time when the sellers and the buyers had been hoping for measures to keep costs down, they say.

Nishith Desai Associates, international legal and tax counselling service providers, point to the clarification in the Budget on the applicability of service tax to renting of immovable property for commercial or business purposes. This amendment has been proposed to take effect retrospectively from June 1, 2007.

### Commercial Property

This clarification overrules the principle laid down by the Delhi High Court in Home Solution Retail India Ltd. V Union of India (UOI) and Ors., wherein it held that the 'act of renting property could not be treated as service'. Pursuant to this judgment, renting of immovable property was considered to be out of the purview of service tax.

As the amendment takes effect from an earlier date, the occupants may now face interest levy or penalty. This will have a significant impact on a wide variety of sectors.

In addition, the Budget also seeks to impose service tax by expanding the scope of the term 'renting'. This term will now include renting of vacant land where there is an agreement between the lessor and lessee for undertaking the construction of buildings for furtherance of business. This will impact the real estate sector, where such agreements are a common phenomenon.

### Healthcare

The Budget also proposes service tax on hospitals, nursing homes and multi-specialty clinics in relation to health check-ups or preventive care services rendered to employees of business entities. It has to be noted that service tax is applicable to such services irrespective of whether the payments are made by the recipient of such service or by an insurance company directly, according to Nishith Desai Associates.

### Residential units

According to developers, the Budget also clarifies that sales of residential property during the construction phase will attract service tax on the construction cost. Developers have expressed dismay over this move which they had thought had been resolved last year when the Central Board of Excise and Customs (CBEC) had clarified that it does not attract service tax.

In the clarification dated January 29, 2009, in the context of service tax of 12 per cent levied with effect from June 1, 2005, on construction of residential complex, the CBEC had said that the initial agreement between the developers and the ultimate owner is in the nature of 'agreement to sell.' This, as per the provisions of the Transfer of Property Act, does not by itself create any interest in or charge on such property. The property remains under the ownership of the seller — the promoters, builders or developers.

It is only after the completion of the construction and full payment of the agreed sum that a sale deed is executed and the property gets transferred to the ultimate owner — the buyer of the residential unit. Therefore, till the execution of such a sale deed, any service provided by the seller in connection with the construction of residential complex would not attract service tax.

Mr K. Vaitheeswaran, an advocate and tax consultant, says the Finance Bill 2010 has introduced an amendment in the form explanation to the definition of taxable service of construction of complex services. The word 'service' has been omitted from the definition and it says construction intended for sale by the builder before or during or after construction shall be deemed to be a service provided by the builder to the buyer. The concept of self-service has been legislatively nullified.

Service tax will not apply only if the buyer makes the entire payment for the property after the completion of the construction, including getting certification by the local authorities.

Typically, according to developers, this will mean an additional Rs 150-200 to the cost of a square feet of built-up space priced around Rs 3,000.

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(Source: iStockAnalyst )

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