Capital Gains: Taxability?

Dr. Maya Chenoy case:

Facts of the case: The Assessee had purchased a property consisting of Land and Building in Hyderabad. The assessee entered in to a development agreement on 09.03.1995 for construction of flats.

As per the agreement the developer was to be hand over the possession of said land and in turn it had to give 45 percent of the constructed area to the assessee. For this purpose the assessee has to demolish the existing structure on the land. Accordingly, the assessee has demolished the building in 1999 and handed over the vacant land for the development. The builder has commenced the construction in the year 2000 and completed the construction in the year 2001.

Assessee has got 4.5 flats towards her share as per the agreement. The assessee has sold two flats for a consideration. For calculating the capital gains on the transfer of the two buildings the assessee has adopted the value of the property as on 01.04.1981.

The assessing officer is of the view that there are two transactions. According to him, the land given for development in consideration of 4.5 flats constitutes one transaction and flat sold by the assessee out of the consideration received for transfer of vacant land is another transaction.

According to the assessee there is only one transaction which is completed only on the handing over of the owner's share in the newly constructed property. It was contended that the owner's liability for capital gains arises only when she transfers her share in the constructed property to the third party.

The CIT (A) in order concurred with AO order to hold that the assessee had entered in to two different transactions one on transfer of ownership rights over 55percent of the undivided share of land and short term capital gain on transfer of two newly constructed flats.

The learned counsel for the assessee submitted that there were two alternative approaches to the problem. First, the entire transaction starting from the date of development agreement to till the date of sale of flats by the assessee was a single transaction. Second, if it is not a single transaction then it will be split in to two transactions as revenue did – one for the transfer of vacant land and another for the transfer of newly constructed flats. He further contended that if 55 percent of the land was transferred by the assessee on the date of development agreement what was the consideration flowing to the assessee?. According to him, flats given to the assessee could not be considered as a consideration as it was a right to receive the property which was still not in existence. The right per se is a property but then the question would arise what was the value of the property. If it cannot be valued then there is no capital gain.

It was argued that events like handing over the possession of land etc were incidental to the whole transaction. It was argued that if 55 percent was handed over, the land owner and developer became the co-owners of the entire property. Therefore, in respect of the co-owners section 53A of the Transfer of Property Act can not apply. If there was a transfer of 55 percent of the land in favor of the developer, is the developer had any legal right to sell 55 percent? According to him, the developer has no such right. Hence it was contended that the development agreement should be viewed as a license only which becomes irrevocable and can be terminated only in terms of license (Development Agreement).

The whole issue revolves around these points. They are:

- Does the development agreement have the effect of transferring the land from the assessee to the buyer under any of the clauses in section 2(47) of the Income Tax Act, 1961?
- Do the events starting from the date of executing the development agreement up to the date of sale of flats by the assessee constitutes one single transaction, or they two separate transactions of land as one transaction and sale of flats as the other?

The Tribunal proceeds to adjudicate the issue as follows:

Section 2(47) defines the term “Transfer”. This definition is inclusive and not exhaustive.

The first clause of the section talks about sale, exchange or relinquishment of the asset.

Under the Transfer of Property Act “Sale” is defined as transfer of ownership in exchange for a price paid or promised to be paid or part paid or part promised. The term “Price” is not defined in the Transfer of Property Act. However, as per Sale of Goods Act it means money consideration for the sale of goods. Thus, the presence of money consideration is essential in a sale transaction. In the present case, there is no money consideration flowing from the developer to the assessee and hence it is not a sale transaction.

Relinquishment means takes place when one person gives up, abandons or surrenders his interest. After the relinquishment, it is owned by a other person other the one who relinquished the property. In this case, the assessee has not surrendered, abandons the property.

Thus it is a case of exchange. Tribunal also held that the argument of learned counsel is that by transferring 55 percent of land to the developer, the latter become the co-owner of the property. However in our view, this could be true if the whole of the property is held by the owners. In the present case, whole of the property was owned by the assessee and out of the whole property; she transferred 55 percent of the land to the developer. By parting away with a part of the property, the transferee does not become co-owner but acquires interest only in the 55 percent of the land transferred to him.

Tribunal further held that, in CIT VS PODAR CEMENTS (p) Ltd case Supreme Court while considering the concept of "Ownership" in the context of section 22 of the Income Tax made certain observations and in our view, these principles are also equally important in the context of capital gains also. Those observations are:

The full rights of the OWNER are:

- The power of enjoyment.
- Possession which includes the right to exclude others.
- Power to alienate inter vivos or to charge as security.
- Power to leave the res by will.

The court added that one of the most important of these powers is the right to exclude the others. The property right is essentially a guarantee of the exclusion of other persons from the use or handling of the thing.

The clause 12 of the agreement provides that the developer shall along with the structure also sell, transfer, convey, gift or otherwise alienate to third parties the undivided share of the land on which building stands. The assessee is not given such right, leave aside anybody else.

The very principle of section 53A of Transfer of Property Act is to provide a shield of protection to the transferee to remain in possession against the original owner who has agreed to transfer the land. As per the Mulla's Transfer of Property Act (2005, 10th Edition) the following postulates are pre requisite for basing a claim on 53A of the TP ACT:

- There must be a contract to transfer for consideration any immovable property. In this case, there is a contract to handover possession of immovable property for a consideration of 4.5 flats.
- There contract must be in writing and signed by the transferor or on his behalf.

- The writing must be in such words from which the terms of necessary to construe the transfer can be ascertained.
- The transferee must in part performance of the contract take possession of the property or any part thereof. In this case developer has taken the possession of the property.
- The transferees have done some act in furtherance of the contract. In the present case, the developer has constructed flats as stipulated in the agreement. Thus, he has performed his part of the contract.
- The transferee must have performed or be willing to perform his part of the contract.

Absolute ownership is an aggregate of component rights such as right of possession, the right of enjoying the right over the land and so on. These subordinate rights, the aggregate make up absolute ownership, are referred in Transfer of Property Act as interest in the property. Sec 5 of the Transfer of Property Act contemplates that the transfer of property either a transfer of absolute ownership, or transfer of one or more subordinated rights.

Sec 5 of the Transfer of Property talks about only transfer and not necessarily transfer for consideration only.

Further, section 53A of the Transfer of Property Act does not debar a person from taking advantage of that section merely because he has not paid the amount in full.

A transfer of property not in existence operates as a contract to be performed in future, which is enforceable as soon as the property comes in to existence.

Therefore in light of foregoing discussions, we are of the considered opinion that the development agreement in the present case has the effect of transfer as contemplated in section 2(47) of the Act.

ITAT, HYDERABAD 'A' BENCH

DR. MAYA SHENOY

VS

ASSISSTANT COMMISSIONER OF INCOME TAX (2009) 124 TTJ (HYD) 692.