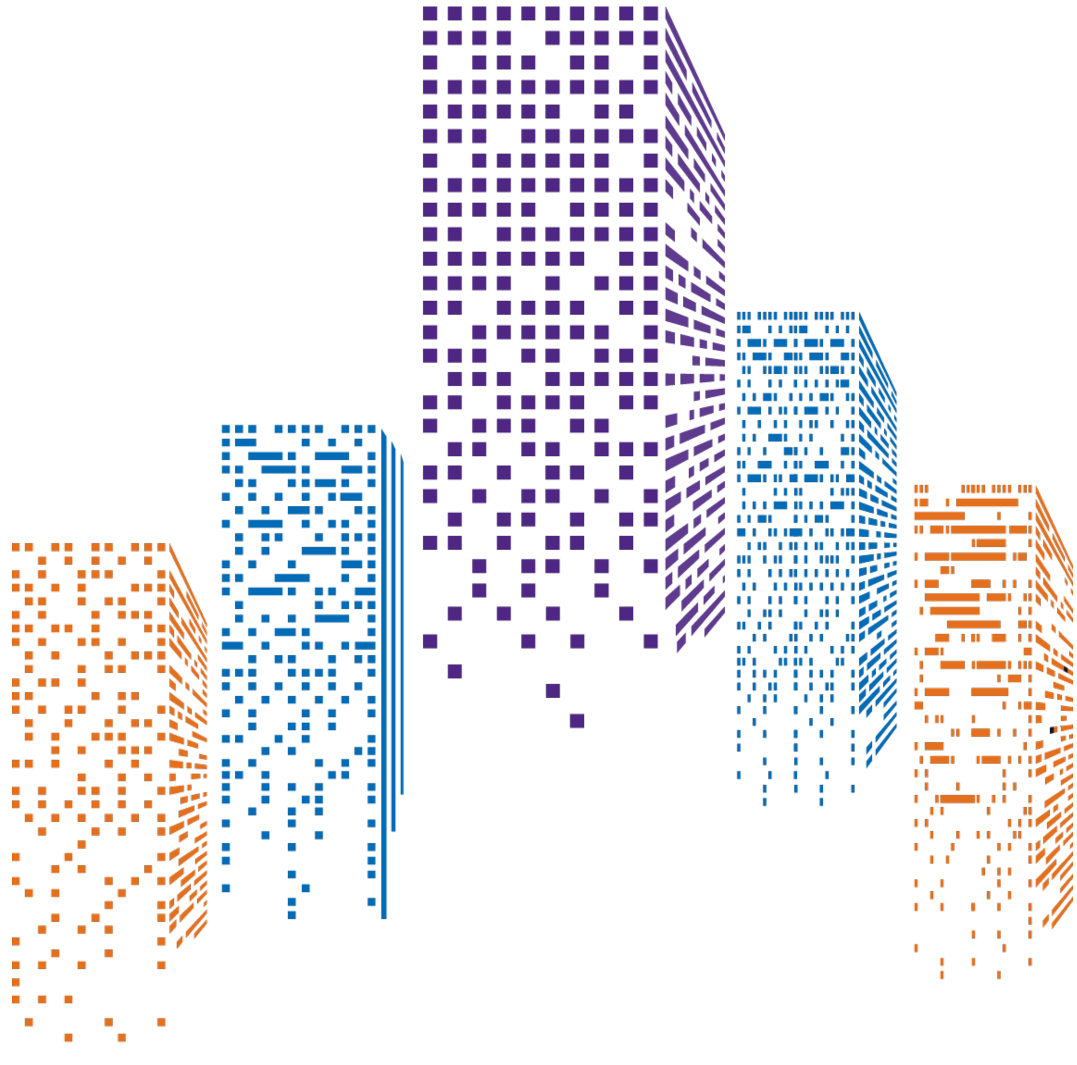
Union Budget 2016-17

Impact on the real estate and infrastructure sector

Contents

01	Foreword
02	An overview
03	Key challenges
04	Growth drivers
05	Key policy initiatives
06	Direct tax proposals
07	Indirect tax proposals



Foreword

Neeraj Sharma
Director, Grant Thornton Advisory Private Limited

Budget 2016 presents a balancing act for the Real Estate and Infrastructure sector. While some of the long pending demands on giving the industry status to the real estate sector, providing single window clearance, etc. are yet to be fulfilled, there has been an attempt by the Government to create demand for real estate. This has been done by raising the exemption limits for the first time home buyers with an overall ceiling of loan/price of property and at the same time, introducing various tax sops/exemptions in terms of income tax and service tax to provide affordable housing and generating supply.

REITs finally get complete exemption from the DDT; this will help companies with quality commercial real estate to monetise these assets.

The focus on infrastructure is kept intact through an enhanced budget on road, railway connectivity etc. These will act as enablers for the real estate sector in the long run. Lastly, announcement of digitisation of land records is a move in the right direction to enhance the transparency and easy accessibility of the land records.

An overview

Real estate and Infrastructure sector has been sluggish in the last few years. Infra projects continue to show significant delays on the completion front due to multiple reasons which include lack of funds and on-going disputes on the real estate front. The residential space continues to face headwinds in the form of muted sales and subdued consumer demand. Against this, commercial real estate market recovered, with improvements in both demand and supply.

Year 2015 witnessed a number of government initiatives to further push reforms for which the blueprint was prepared in 2014 itself.

- Relaxation of foreign direct investment (FDI) norms,
- Clarifications around the Real Estate Investment Trusts (REITs),
- Approval of the Real Estate (Regulation and Development) Bill by the Cabinet.
- Launch of Smart City – Announcement of first 20 cities to be developed under Smart Cities Mission

Key challenges

Delays in project completion leading to cost and time overruns

Scarcity of developable land

Availability of cheap finance

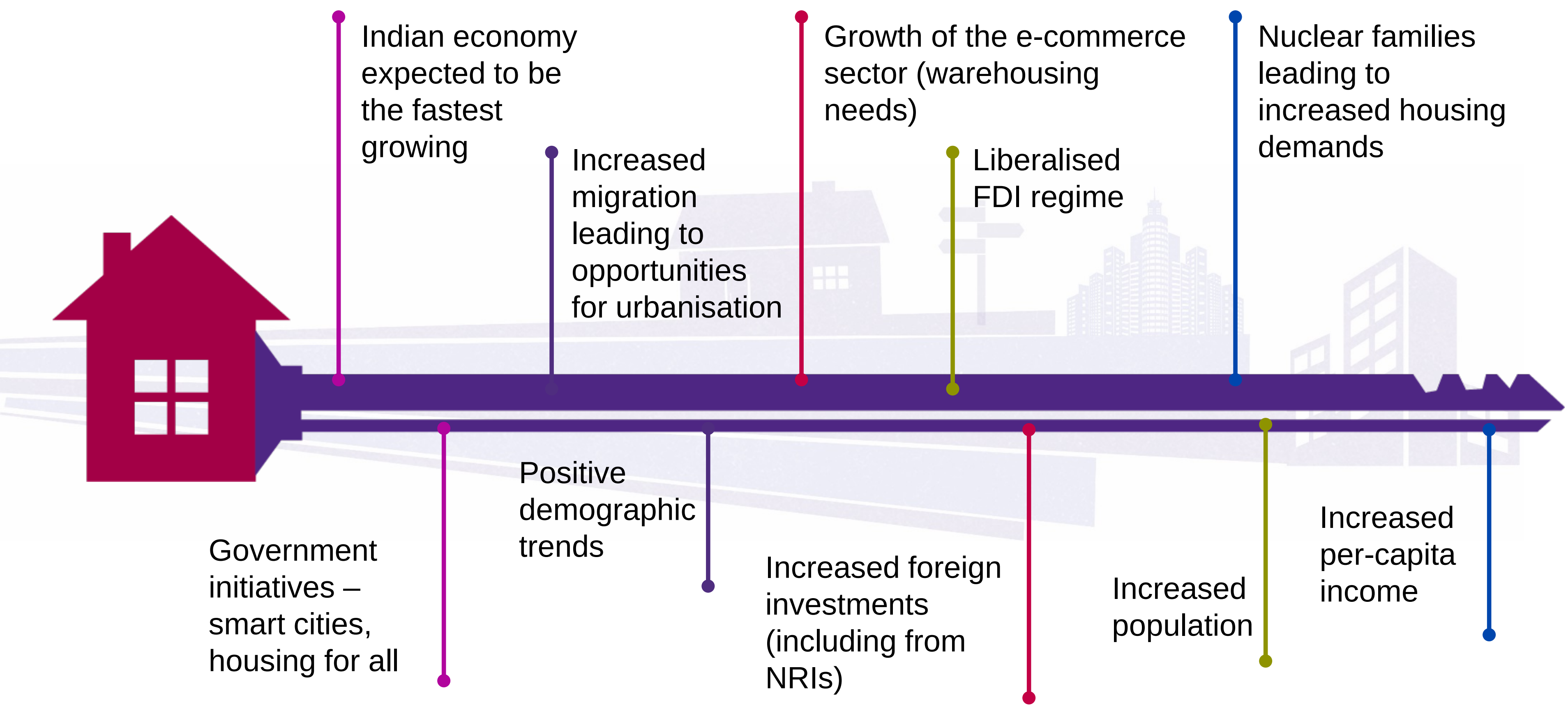
Slowdown in the global economy has led to a deceleration in the real estate and Infrastructure sector

Single window clearance mechanism not in place

Setting up of a real estate regulator

Inability of the builders to lower prices

Growth drivers



Key policy initiatives

Real Estate (Regulation and Development) Bill

Union Cabinet in December 2015 approved the amended draft of the Bill. Some of the significant provisions of the Bill are:

- The legislation covers all residential and commercial projects over 500 sq. mt. area or with a minimum of eight apartments
- The Bill requires the developers to keep 70% of the project cost, which includes the land cost, in a dedicated account
- As against the practice of builder-drawn sale agreements being heavily tilted in favour of developers, the legislation provides for a Model Agreement, which shall be the basis of all transactions

Foreign Direct Investment (FDI)

The Department of Industrial Policy and Promotion (DIPP) introduced amendments to the Consolidated FDI Policy. Some of the key amendments are:

- The minimum floor area requirement of 20,000 sq. mt. to be eligible for FDI has been removed
- The minimum capital requirement of US$5 mn which had to be provided within six months of commencement has been removed
- Exit clause has been simplified as each phase of the construction project will be considered a separate project for the purposes of the FDI exit

Key policy announcements

Outlays on infrastructure

- Capital expenditure of the Railways and roads will be Rs 2,18,000 crore in FY 2016-17
- Total outlay for infrastructure is Rs 2,21,246 crore
- Central Government to draw a plan to revive 160 unserved or underserved airports to enhance local connectivity
- An initiative has been made to transition into a new credit rating system for infrastructure projects which will enable correct risk analysis of the projects, resulting in efficient loan funding

Digitisation of land records

- This initiative would now be part of the Central Government project with a fund allocation of Rs 150 crores

Shop and establishment act

- Shops outside the malls would get an opportunity to choose to operate all seven days of the week. A model shop and establishment act shall be circulated by the Central Government, which can be voluntarily adopted by the States. The law would have safeguards to protect the interest of the workers, in terms of mandatory weekly holiday, number of working hours per day, etc.

Direct tax proposals

Individuals

- Tax slabs remain unchanged
- Surcharge increased from 12% to 15% for individuals with total income exceeding Rs 1 crore (increasing effective marginal rate for super-rich to 35.535% from 34.608%)

Corporates

- Tax rate reduced by 1% to 29% for domestic companies with a total turnover/gross receipts of upto Rs 5 crore in FY 2014-15

Other assessees

- No change in tax rates and surcharge for firms, Limited Liability Partnerships and co-operative societies

Increase in tax rates for the super-rich and slight reduction in corporate tax rates for small companies

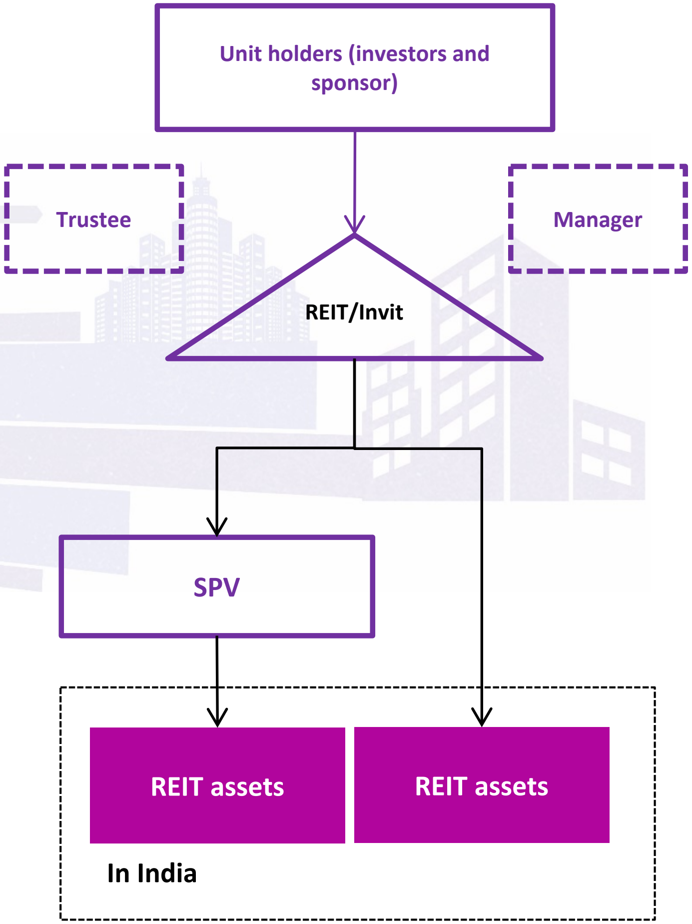
Direct tax proposals

REIT /Invits SPVs exempted from Dividend Distribution Tax

The Real Estate Investment Trust (REIT) or Infrastructure Investment Trust (Invit), in accordance with the Securities and Exchange Board of India (SEBI) Regulations are permitted to hold assets directly or through an SPV which can take form of a company or LLP.

The amendment brings parity between the dividend income vis-à-vis interest or rental income from the SPV being a company, wherein the REIT/Invit holds specified shareholding and fulfilling other conditions, by doing away with the DDT on distributions of dividend by SPVs.

This would be of significance bearing in mind that SPVs are obligated to distribute minimum 90% of their operating income under the SEBI Regulations.



Direct tax proposals

Affordable Housing

Section 80-IBA proposes to provide 100% deduction of profits to an undertaking from a housing project comprising of units up to 30 sq. metres(323 sq.ft) in four metro cities and 60 sq. metres(646 sq.ft) in other cities.

- Land size for project: Plot of the land to measure not less than 1000 sq. metres(10,764 sq.ft) in the aforesaid metro cities or 2000 sq.metres(21,528 sq.ft) in other cities
- Utilisation by project of the floor area ratio permissible: not to be less than 90% in aforesaid metro cities (80% in other cities)
- Built-up area of the shops and other commercial establishments (within project): only upto 3% of the total built up area

If a residential unit is allotted to an individual, no other residential unit in the housing project shall be allotted to the individual or the spouse or the minor children of such individual.
Approval for the project to be procured during June 2016 to March 2019, and project to be completed within three years of the approval. The deduction is subject to various other conditions. Minimum Alternate Tax will, however, apply to these undertakings.

It may be noteworthy that the eligible unit size in the erstwhile profit based deduction for affordable housing, was much larger. The profit based deduction to the affordable housing sector in the new avatar should increase interest of developers to construct affordable housing projects and help in contributing in the "Housing for All" scheme.

Direct tax proposals

Individual tax

Deductions in respect of rent paid

In case of an individual not receiving house rent allowance from his employer, a deduction of Rs 2,000 per month or 25% of his total income, whichever is lower, is currently available in respect of rent paid in excess of 10% of his total income.

The limit of Rs 2,000 per month is proposed to be increased to Rs 5,000 per month from FY 2016-17 onwards.

Incentivising first time home buyers

Additional deduction is proposed upto Rs. 50,000 for interest on loans (sanctioned between 01 April 2016 and 31 March 2017) upto a maximum of Rs 35 lakhs where the value of the house property purchased does not exceed Rs 50 lakhs.

Direct tax proposals

House property

Increased time frame for pre acquisition/construction interest on self-occupied house property

Deduction of interest incurred before the acquisition or construction of a self occupied house property is available presently if the acquisition or construction of such house property is made within 3 years from the end of the financial year in which loan is availed. This is now proposed to be increased to 5 years.

Amended section 25A to subsume tax treatment for unrealised rent and arrears of rent

Provision for taxability of arrears of rent and unrealised rent has been consolidated and subsumed under amending section 25A. The amended section continues to tax arrears of rent or recovery of unrealised rent on receipt basis irrespective whether the assesse is the owner of the property or not in the FY of receipt.

Standard deduction @ 30% allowable in year of taxation on receipt basis on both unrealised rent or the arrears of rent.

Direct tax proposals

Capital gains

Deemed minimum consideration: date of agreement vs. date of registration of transfer

Presently when an assessee claims that value adopted by stamp authority as on the date of registration of transfer of a land and/or building exceeds the transaction value, the value adopted by stamp authorities would be deemed as the consideration for transfer for computation of capital gains.

It is proposed to provide that in case date of agreement for the transfer (fixing the amount of consideration) and the date of registration are different, the stamp value as on the date of agreement may be taken as full value of consideration for the purposes of computation of capital gain. This shall apply only if whole of the transaction value or part thereof has been paid through accounts payee cheque or bank draft or electronic clearing system before date of agreement for transfer.

This is an anti-abuse provision to make stamp duty value as the minimum consideration for taxing capital gain. The amendment is brought about to give latitude to transactions where the stamp value have increased between the period of agreement to sell and the registration of transfer. Similar provisions exist in the Act with respect to sale of immovable property being stock in trade and deemed income from other sources on receipt of immovable property below the fair market value.

Direct tax proposals

Proposed phase out of incentives :

Section	Particulars	Current incentive	Proposed phase out of incentives
10AA	Tax holiday on export income of SEZ units	15 year tax holiday without a sunset clause	Sunset clause introduced i.e. applicable only to those SEZ units that commence operations prior to 31 March 2021
35AD	Investment linked deduction for the purchase of machinery and other capital assets (100% or 150% in various cases) for specified businesses, e.g., cold chain facility, warehousing facility for storage of agricultural produce, an affordable housing project, production of fertilizer, hospitals	Weighted deduction of 150% of capital expenditure *(other than expenditure on land, goodwill and financial assets)*	100% of capital expenditure w.e.f. FY 2017-18

With a sunset clause introduced for benefits available to a SEZ unit, taxpayers now have only a window of little over 5 years to set up a new SEZ unit.

Even the investment based deduction available to specified infrastructure facilities are being phased out.

Indirect tax proposals

Service Tax

Krishi Kalyan Cess

- Krishi Kalyan Cess is proposed to be introduced at the rate of 0.5% on all taxable services w.e.f. 01 June 2016
- Input credit of Krishi Kalyan Cess would be available

Amendments to the mega exemption list

- Certain amendments have been proposed to the mega exemption list of services w.e.f. 1 April 2016:
  - Construction, erection, commissioning, installation of original works in relation to mono rail and metro where contracts executed subsequent to 01 March 2016 now considered as a taxable service (Taxable value of service @ 40%);
  - Exemption granted to services by way of construction etc. in respect of:
    (i) housing projects under Housing For All (Urban) Mission/ Pradhan Mantri Awas Yojana (PMAY);
    (ii) low cost houses up to a carpet area of 60 square metres in a housing project under “Affordable housing in Partnership” component of PMAY;
    (iii) low cost houses up to a carpet area of 60 square metres in a housing project under any housing scheme of the State Government, are being exempted from Service Tax
  - Original works in relation to airports and ports exempted up to 01 April 2020 for contract executed prior to 01 March 2015

Service tax under reverse charge mechanism

- Service recipient to discharge service tax w.e.f 01 April 2016 with respect to all services provided by Government or local authority other than those specifically excluded

Indirect tax proposals

Service Tax

Service provided to Government by way of construction etc. of:

- a civil structure for use other than for commerce, industry or any other business or profession
- a structure for use as educational, clinical, art or cultural establishment
- a residential complex meant for self-use or for employees

  wherein contract already entered and appropriate stamp duty paid before 1 March 2015 with sunset date 31 March 2020

Services provided by way of construction of original works pertaining to canal, dam or other irrigation works

- Services provided by way of construction of original works pertaining to canal, dam or other irrigation works has been exempted w.r.e.f. 01 July 2012
- Refund of such service tax paid is allowed as refund in certain cases and has to be filed within 6 months from the date on which the Finance Bill, 2016 is enacted

Rationalisation of interest rates

- interest rates rationalised and reduced from existing slab rates of 18/24/30% to 15%

  - in cases of service tax collected but not deposited, interest rate to be 24%
  - subvention of 3% to small service providers with revenue up to Rs. 60 lacs

Indirect tax proposals

CENVAT Credit Rules

Amendments to the mega exemption list

- For the purpose of CENVAT reversals under Rule 6 of the CENVAT Credit Rules, 2004 ('CCR') following changes have been proposed w.e.f. 01 April 2016:
  - Exempted services includes an activity, which is not a service (example: trading of goods)
  - Option of maintaining separate books has been replaced with specified methods depending on the nature of output activity
  - 2 year condition imposed on CENVAT credit eligibility on capital goods exclusively attributable to exempted activity
- Reversal under Rule 6 of CCR

Rule	CENVAT credit attributable to	CENVAT credit availability
6(1)	Exclusively exempted goods / services	Not allowed in entirety
6(2)	Exclusively non-exempted goods / services	Allowed in entirety
6(3A)	Common CENVAT credit	To be reversed in the ratio of exempted turnover to sum of exempted and non-exempted turnover for the pervious financial year *

**where no activity is done in the previous FY, then CENVAT credit should be reversed to the extent of 50% of common credit*

- Monthly reversal basis PY's turnover required to be done,
- Interest rate for non-reversal of CENVAT credit reduced to 15% pa from 24%.

Indirect tax proposals

Central Excise

Central Excise rate on ready mix concrete manufactured at the site of construction for use in construction work at such site, reduced to NIL w.e.f. 01March 2016

Contact us

To know more, please visit **www.grantthornton.in** or contact any of our offices as mentioned below:

NEW DELHI National Office Outer Circle L 41 Connaught Circus New Delhi 110 001	**AHMEDABAD** BSQUARE Managed Offices, 7th Floor, Shree Krishna Center, Above Crossword, Nr. Mithakali Six Roads, Navrangpura, Ahmedabad 380009	**BENGALURU** "Wings", 1st floor 16/1 Cambridge Road Ulsoor Bengaluru 560 00	**CHANDIGARH** B-406A, 4th Floor, L&T Elante office Industrial area, Phase-I Chandigarh – 160002	**CHENNAI** Arihant Nitco Park, 6th floor No.90, Dr. Radhakrishnan Salai Mylapore Chennai 600 004
GURGAON 21st floor, DLF Square Jacaranda Marg DLF Phase II Gurgaon 122 002	**HYDERABAD** 7th floor, Block III White House Kundan Bagh, Begumpet Hyderabad 500 016	**KOCHI** 7th Floor, Modayil Centre point, Warriam road junction, M.G.Road, Kochi 682016	**KOLKATA** 10C Hungerford Street 5th floor Kolkata 700 017	**MUMBAI** 16th floor, Tower II Indiabulls Finance Centre SB Marg, Elphinstone (W) Mumbai 400 013
MUMBAI 9th Floor, Classic Pentagon, Nr Bisleri, Western Express Highway, Andheri (E) Mumbai 400 099	**NOIDA** Plot No. 19A, 7th Floor Sector – 16A, Noida – 201301	**PUNE** 401 Century Arcade Narangi Baug Road Off Boat Club Road Pune 411 001		

For more information or for any queries, write to us at **contact@in.gt.com**

Follow us @GrantThorntonIN