

Doha Chapter of ICAI

5th January 2014

**Relevant Changes in FEMA regulations and Direct & Indirect Taxation
affecting Real Estate Transactions,
with reference to NRI**

**by CA R.BUPATHY
PAST PRESIDENT - ICAI**

EXECUTIVE SUMMARY FEMA Regulations

Introduction

The Indian Government recognises the importance of Indian Diaspora, NRIs (Non-resident Indians) and PIOs (Persons of Indian origins) who despite being away from India is making her shine on a global platform, by bringing in economic, financial, and global benefits to India.

The foreign exchange remittances, investment and repatriation are governed by various legislations in India. It is important to understand the changing legislations to avoid future legal tangles, as the Govt has quicker access to information.

Property acquisition, disposal and remittance are governed by general and specific permission of the Reserve Bank of India. However, any person residing abroad cannot indulge in real estate business in India.

ACQUISITION:

- *Non Resident Indians (NRIs) / Persons of Indian Origin (PIOs) can acquire by purchase, gift or inheritance, immovable property in India other than agricultural land/ plantation/ farm house, under general permission.*
- *To acquire agricultural land, plantation and farm house prior permission of RBI is required, except by way of inheritance.*

- *While acquiring under general permission, NRI/PIO cannot register with a Foreign National of Non-Indian Origin as a Joint holder except with approval of RBI.*

DISPOSAL:

NRI/PIO have general permission for disposal except in the following cases and conditions, where RBI approval is required.

- *NRI/PIO cannot gift agricultural land, plantation and farm house except to a resident and a citizen of India.*
- *An NRI/ PIO cannot sell or gift any immovable property to a Foreign National of Non-Indian Origin.*
- *Further, a PIO cannot sell/gift to another PIO without prior RBI approval.*

REPATRIATION:

Repatriation of sale proceeds of property under general permission;

- *Acquired as a NRI cannot exceed the investment made through direct remittance by banking channels, and payments from NRE/FCNR account.*
- *Permitted upto only two residential properties*
- *The Sale proceeds may be credited to NRE a/c only, so that the repatriation limit of 10 lakh USD per annum on NRO a/c will not apply.*

Sale Proceeds from property acquired as a resident and from gifted/inherited property to be credited to NRO a/c only.

- *Repatriation limit per financial year is fixed at 10 lakh USD.*
- *This is subject to obtaining a certificate from a chartered accountant in Form 15CB certifying that due income tax has been paid.*
- *Form 15CA refers to the particulars to be given by the assessee.*

Refund of cancelled bookings

NRIs / PIOs are allowed refund of application/ earnest money paid to the house building agencies/ seller on account of non-allotment of flat/ plot/ cancellation of bookings/ deals in respect of purchase of residential, commercial property, together with interest, if any, subject to deduction of tax at source.

Rental receipts from renting of immovable property can also be repatriated by an NRI/PIO. The rental receipts can be credited to NRO a/c only, subject to payment of taxes, and it cannot exceed the annual limit of 10 lakh USD.

General Permission to repatriate current income

Powers have been delegated to the Authorised Dealers to allow repatriation of current income like rent, dividend, pension, interest, etc. of NRIs/PIO who do not maintain an NRO account in India based on an appropriate certification by a Chartered Accountant in 15CB, certifying that the amount proposed to be remitted is eligible for remittance and that applicable taxes have been paid/provided for.

Recent Changes in issue of CA certificate

*The person responsible for making **any payment to a non-resident**, not being a company, or to a foreign company shall furnish the following information to an authorized dealer as per Section 37BB of the Income Tax Act, namely:—*

- (i) the information in Part A of Form No.15CA, if the amount of payment does not exceed fifty thousand rupees and the aggregate of such payments made during the financial year does not exceed two lakh fifty thousand rupees;*
- (ii) the information in Part B of Form No.15CA , if the payment is not chargeable to tax and is of the nature specified in column (3) of the specified list ;*

- (iii) *the information in Part C of Form No.15CA for payments other than the payments referred in clause (i) and clause (ii) after obtaining—*
- (a) *a certificate in Form No. 15CB from an accountant; or*
 - (b) *a certificate from the Assessing Officer; or*
 - (c) *an order from the Assessing Officer.*

The information in Form No. 15CA shall be furnished by the person electronically to the website designated by the Income-tax Department and thereafter signed printout of the said form shall be submitted to the authorised dealer, prior to remitting the payment.

The above changes in Form 15CA and 15CB is applicable from 01/10/2013 onwards.

Loans for purchase and repairs of property

An NRI/PIO can avail loan for purchase and repairs not exceeding Rupees 100 lacs against NRE/FCNR Deposits. Also mortgage is permitted. Such loans can be repaid in the following manner:

- (a) by way of inward remittance through normal banking channel or*
- (b) by debit to the NRE / FCNR (B) / NRO account of the NRI/ PIO or*
- (c) out of rental income from such property*
- (d) by the borrower's close relatives, as defined in section 6 of the Companies Act, 1956, through their account in India by crediting the borrower's loan account.*

*A **Foreign National of Non-Indian Origin** can only inherit any immovable property including agricultural land/ plantation /farm house. All other activities will need RBI approval.*

DIRECT TAXES

Income Tax

All income generated in India except for the interest on NRE and FCNR accounts are taxable in India for a non-resident. To recover the tax on the income, the Government looks to tax deduction at source (TDS). It places an onerous responsibility on the payer to deduct and promptly deposit prescribed taxes on specified payments and file quarterly TDS returns. In the process, there is the necessity to obtain PAN to execute certain transactions. Failure in complying results in liability to interest, penalty and even prosecution.

PURCHASE AND SALE OF IMMOVABLE PROPERTY

TDS is a legal compliance to be followed during purchase and sale of immovable property.

Section 194IA – *On the purchase of property by an non-resident from a resident seller, tax has to be deducted @1% on the sale consideration in excess of Rs.50 lakhs from 1st June 2013. The procedure for tax payment is simple. The purchaser has to pay tax through Form 26QB which is a challan-cum-statement, and issue a TDS certificate under new Form 16B. While PAN of resident seller is necessary, no TAN for deductor is required.*

- *If seller does not provide PAN, the deduction is @20%.*
- *There is no obligation to file a TDS return.*

Section 195 – *On sale by a non-resident, the person purchasing the property is under an obligation to deduct tax at source @ 20% on the sale consideration. TAN of deductor and PAN of seller is required. Where lower rate is applicable, application under section 195(2) can be filed by purchaser with Income Tax Department and permission obtained.*

Alternatively, the NRI can also make an application under section 195(3) for nil/lower TDS, giving details of the capital gains and proposed reinvestment, pursuant to which the assessing officer will determine the capital gains and issue a certificate for nil/lower TDS as the case may be.

TDS returns have to be filed online and TDS certificate (Form16A) is to be issued.

The TDS certificate can be downloaded from TRACES (www.tdscpc.gov.in).

Advance Tax

Advance tax may be paid by a non-resident purchaser to avoid interest on non-deduction of TDS.

CAPITAL GAIN

On sale of immovable property, the resulting capital gain is taxable under section 45 of the Income Tax Act, 1961. The indexed cost of acquisition, indexed cost of improvement and expenses incurred for the purpose of transfer can be deducted to compute capital gains.

Exemptions from capital gains can be claimed u/sec 54, 54F to the extent of investment in acquiring a residential house /deposit in a Capital Gain Account Scheme (CGAS), provided the asset transferred is a Long Term Capital Asset (LTCA)(held more than 36 months).

- *Section 54 applies to transfer of a residential house and Section 54F applies to transfer of any LTCA other than a residential house.*
- *The above sections provide relief to the extent of capital gain used in the purchase or construction of a residential house property, however not limited to one house property.*

- *The purchase should be made within one year before, or within 2 years after the date of transfer of the residential house property. The construction should be completed within 3 years from the date of transfer or residential house property.*
- *Any unused sum can be deposited in CGAS before the due date of filing return, and used within the specified time limit.*
- *Where the newly purchased /constructed property is transferred within 3 years, the exemption granted is revoked, and the capital gain is taxed.*

Joint Development of Property

Joint Development agreements should be carefully drafted incorporating all specified legal requirements such as date of transfer, the ratio of sharing and the accruing sale consideration. Even arrangements confirming privileges of ownership without transfer of title constitutes transfer. Ascertaining the date of Transfer assumes great importance, as a consequent liability flows to the Property Owner by way of payment of capital gains tax in the year of transfer.

Sale Consideration not ascertainable Section 50D

In situations, where the consideration received or accruing as a result of the transfer of capital asset is not ascertainable or cannot be determined, Section 50D provides that for the purpose of computing capital gain, the fair market value of the asset transferred shall be deemed to the full value of consideration. This section was inserted by the Finance Act, 2012 with effect from 01.04.2013.

Sale Consideration being less than Stamp Duty Guideline Value

In instances where the immovable property is sold for a consideration less than the stamp duty guideline value, the difference is taxed as Capital gain in the assessment of the Transferor.

Further Section 56 of the Act, has been amended to provide that in such situations, the difference will be treated as gift received by the Transferee and taxed as income from other sources. This amendment is introduced by the Finance Act, 2013, effective from 01.04.2014.

Concept of Reverse Mortgage : *Any resident Indian citizen above the age of 60 years may mortgage the residential property under self occupation, for the purpose of earning an income for self sustainability, either as lump sum or monthly receipt. No repayment of the mortgage (principal or interest) is required until the borrower dies or the home is sold. The legal heirs have the option of repaying the mortgage without selling the property. These type of mortgages have high organization costs added to the initial loan amount and hence borrowers with better credit worthiness should check for other loan options as well.*

Wealth Tax Provisions

Documents to be maintained:

- **by a purchaser of flat .**

Other than the Original Sale Deeds towards UDS, the builder's agreement mentioning all the construction cost upto handing over, the cost of improvements and additions to building –contract bills and payments made. These details will help factor the cost to determine the indexed cost of acquisition and improvement to compute the capital gain arising on the future sale of the immovable property.

Also Corporation receipts, Completion Certificate, Bank Statements also to be maintained.

- **by a purchaser of Independent Residential House**

The owner will have to maintain the following records such as parent document, Encumbrance Certificate, Corporation tax/Water tax receipts, approved plan, legal opinion.

INDIRECT TAXES

Service Tax

Construction services attract service tax @ 12.36%. However, the service tax liability is of the Builder/Developer, which he may choose to recover from the purchaser. Hence, it is important to understand the different conditions under which the levy is attracted.

Purchase of under construction flat

Where any person enters into a Builder's agreement or an Agreement for Sale of flat with a Developer/Builder, which requires him to make any payment, such as booking or advance payment, and thereafter construction linked payments that are made from time to time, service tax is attracted on all payments except the payment towards land or UDS.

Purchase of constructed flat

Only in cases where a constructed flat is acquired, no service tax is payable, provided the entire consideration is paid after issue of completion certificate.

Construction of an independent house

Also, where an independent house is constructed there is no liability to service tax.

Construction of flats

Where an individual constructs two or more flats for sale, it will attract service tax. However, the levy is on the contract payments made to the contractor/builder.

Joint Development of property

In the case of Joint Development agreement entered by land owner with Developer/Builder, construction service is provided to the land owner, and service tax is payable on the consideration paid to the Developer. Where the proportionate land (UDS) is transferred in lieu of the transfer of built up flats by the developer/builder, the sale consideration of similar flats sold will be taken as the consideration to the Developer/builder on which service tax is payable. Abatement upto 75% can be claimed where the consideration is a lump sum payment including the value of land.

Let-out Property

House property let out for residential purposes is not liable to service tax. However, commercial let out properties are liable to service tax. A basic exemption limit of Rs.10 lakhs has been provided. Once the limit is exceeded during any financial year, the tax levy applies and thereafter service tax is payable every year whether or not the gross income is greater or lesser than the limit. Once the income exceeds Rupees 9 lakhs registration has to be taken. Application can be filed under Form ST-1 online and thereafter the hard copy of attested documents needs to be filed with the jurisdictional service tax Department. Copy of passport, PAN attested by the Indian Embassy is to be submitted. Copy of Municipal Taxes Receipts, Copy of Rent Receipts, Copy of Bank Statement, Copy of Electricity Bill, Copy of Telephone Bill should be made available by NRI, if called for. The registration can also be taken through a valid Power of Attorney. Due care has to be taken to draft the Rental agreement mentioning the liability to service tax as and when it becomes applicable.

CONCLUSION

We may thus conclude that in the present economic conditions prevailing in India, there is an increasing bundle of investment opportunities being thrown open for foreign investment in India through regularised channels which can be utilised by our community residing abroad to their best interests subject to knowing and following the rules and regulations in place and compliance requirements.