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Tax reform good for Indian property

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The implementation of the Goods and Services Tax (GST) should further enhance India's attractions as an investment destination by encouraging greater transparency and ease of operation in all property deals. The industrial property and warehousing segment should be the primary beneficiary of adoption of the GST system in the short term, since operating efficiency should increase. It is too early to say whether implementation of the GST will cool down prices in the commercial and residential segments as the GST does not cover immovable property sales, to which stamp duty will continue to apply.

Implications of tax reform favourable

Indian legislators on 3 August approved the long-awaited uniform Goods and Services Tax (GST). Implementation of their decision may take a year or more, but even so most economists agree that adoption of the GST across all Indian states and consequent simplification of the Indian tax system have the potential to stimulate overall economic growth. The measure thus boosts the investment attractions of a country whose 7.5% GDP growth rate and favourable demographic profile (more than 50% of the population is below 25) already make it one of the world's most attractive emerging markets.

More specifically, real estate has to deal with a multiplicity of taxes applicable at different points of the property cycle. These taxes include indirect taxes such as service tax, excise duty, and value added tax (see Figure 1), which apply to the procurement of goods and services during construction, as well as direct taxes such as capital gains tax and wealth tax. Stamp duty is also payable on sales of immovable property. The implementation of the long-awaited GST will bring all indirect taxes under one unified tax structure; leading to a scenario where there will only remain the direct taxes, stamp duty and GST for all property related transactions. This change should help industry in India to move towards more efficient tracking of transactions; it should also reduce tax evasion and augment compliance. Consequently, we foresee an increase in transparency which should provide greater comfort to international investors in the Indian market.

Impact on industrial and warehousing property – Positive

In the short term, the industrial and warehousing property sector should be the chief beneficiary of the implementation of the integrated GST. The decision to establish a warehouse will no longer be based on tax arbitrage, but on achieving the most optimal logistics solution. This will lead to a significant reduction in transport time as we do away with octroi checkpoints. Logistics companies will look to establish large consolidated warehouses located on strategic transit corridors. We should thus see the development of a hub and spoke system of warehousing, the hubs being on transit corridors and the spokes on feeder lines. We thus expect the cost of products to come down and the country to become one truly large market. Further, recent government initiatives such as "Make in India" and 100% FDI in the e-commerce sector should also boost the manufacturing and warehousing sector. Various global players like Amazon, e-Bay etc. have already entered the Indian markets and started occupying large warehouse spaces in order to gain a share of the e-commerce business.

Impact on commercial property sector - Neutral

Commercial leasing constitutes a major portion of overall commercial property business in India. Currently, leasing of commercial property qualifies as a service and thus is subject to service tax. The service tax is applicable at the rate of 15%. After the implementation of GST, we assume that the treatment will remain the same and leasing of commercial property will be subject to GST. The positive or negative impact should primarily depend on the applicable GST rate. Moreover, there is still ambiguity about the availability of GST tax credit paid on procurement of goods and services during the construction phase. The model GST Law states that credit of GST paid on goods and services acquired for construction of immovable property (other than plant and machinery) will not be available. In the event credit is not available, there will not be much difference in the overall tax regime except for greater simplicity.

goods and services.

3. 3. Residential leasing is currently not considered for service tax. This situation is likely to remain the same under the GST regime as well.

Impact on residential property sector - Neutral

It is too early to comment whether the implementation of GST will bring down residential property prices. We have analysed the impact of the GST on three types of residential property transactions, namely: 1) sale of completed immovable property, 2) sale of property under construction, and 3) leasing of residential property:

1. The sale of immovable property should not be impacted by the GST as these transactions will not fall under the ambit of the GST and stamp duty will be payable on these transactions
2. The sale of property under construction should be covered under the GST. However, currently it looks as though there will not be much difference besides the fact that all the indirect taxes will come under one heading. There will be some benefit only if tax credit is available for the developers for the GST paid on

Overall conclusion

In conclusion, we expect the GST to boost demand for real estate, especially in the industrial and warehousing sector due to the positive impact on the economy as a whole. However from a cost perspective, more clarity is required about the applicability of tax credits on various transactions. If there is proper application of the credit utilisation mechanism, then the developers should be able to obtain credit for various taxes paid on inputs which will eventually help reduce their overall costs.

Land Stage	Under Construction stage	Completion Stage	Secondary Sale
Stamp Duty is payable on land purchase. It varies at state level (5 to 9%).	**Service Tax** – 15% on value of services. Paid by developers to the govternment and ultimately borne by buyers. It is calculated on 25% of the total cost of the project.	**Stamp Duty** 5 to 9% on property value and is borne by the buyer.	**Capital Gains Tax** – 20 to 30% depending on holding period
Wealth Tax -1% over the net wealth that exceeds INR 30 lakh (INR 3 million). Applicable for the number of years one holds the property as land.	**Value Added Tax** –4% on all industrial outputs and capital goods. However, for luxury good it is levied at 20% and for others it is 13.5%.	**Property Tax** – 6 to 10% on annual rental value. Water Tax & Sewerage tax is part of property tax in many states	**Stamp Duty** – to be borne by buyer
	Customs Duty on import of goods – varies from **0%** to **150%**, with an average duty rate of **11.9%. (**Any material imported for construction will be levied with the applicable custom duty).	**Wealth Tax** – 1% over the net wealth that exceeds INR 30 lakh (INR 3 million).The tax is to be paid annually on its market value, irrespective of whether such property yields any income.	
	Excise Duty Tax – 12.5% applicable on manufacturing of goods.		

Source: Colliers

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