

Dialogue on GST, Demonetization and the Built Environment Industry

On 16th November 2017, RICS SBE and NIUA organized a Dialogue on GST, Demonetization and the Built Environment Industry at India International center, New Delhi. As part of the dialogue - Prof. Arun Kumar, Malcolm S. Adiseshiah Chair Professor at Institute of Social Sciences, gave a keynote address on “Demonetization and its impact on parallel economy, real estate and construction sector.”

Following the presentation a panel discussion was conducted on the Impact of Demonetization and GST on the built environment sector. The panel discussion was chaired by Prof. Sunil Agarwal, Associate Dean and Director, School of Real Estate, RICS SBE. Among the panelists Prof. Arun Kumar was accompanied by Prof. Jagan Shah, Director - National Institute of Urban Affairs, Mr. Arun Gupta Partner at SARC & Associates, Mr. Prashanth Agarwal – Partner, Indirect Tax, PWC and Mr. Gaurav Gupta, Director - Marketing in SG Estates Ltd.



Keynote Address - Highlights

Prof. Arun Kumar in his presentation discussed how demonetization is just not a blip but has resulted in India’s economy declining for the last six quarters now. According to him, impact of this process had on the informal economy was negative. He argued that the 5.7% growth rate of the economy, quoted by the government does not include the unorganized sector into the account, which is 45% of the India’s economy. If we were to include the unorganized economy in our calculations, the growth rate will be around 1%, which is a point of big concern.

He also stressed that due to demonetization income circulation was negatively affected in the unorganized sector, since it depended on cash for this and didn’t had access to digital banking facilities. Therefore when more than 80% of the cash was withdrawn from the market unorganized segment faced the maximum brunt of this process. Also due to demonetization discretionary spending stopped/ reduced, as a result industrial demand also went down. Falling credit offtake of the banks is a proof that demand in the Indian economy has slowed after demonetization.

Moreover black economy did not get affected as anticipated, by demonetization because black economy is not separate from white economy, it is intertwined with it. They both are generated simultaneously and thus conversion of one to other is very much feasible. Also demonetization failed to hit the process of black income generation. Cash is a small part of black income, and since the mechanism was not affected as a result there was also no impact on black money. Prof. Arun Kumar also pointed that black wealth as far in excess of the currency and is stored in gold, real estate etc. So demonetization was never a solution to bring out black money also it failed to hit the process of black money generation. However Prof. was of the view that demonetization created a positive sentiment and did well for the “Robin Hood” image of the government.



Prof. Kumar also shared his views on GST, he said that GST in the country is billed as the biggest tax reform in India and a game changer, he told that GST is also an indirect tax Just like VAT. As per him many critical issues regarding basic design of GST were not discussed in advance and remain unresolved. GST is introduced in a very complex form and this will make its implementation and compliance difficult, he said our country needs a simple taxation method. He emphasized that major inputs like real estate, petro goods and alcohol have not been brought under GST, due to this the cascading effect on taxation which GST aimed to remove cannot be achieved. Also the small and tiny units producing and selling locally would lose from a unified market which will benefit the large scale producers, this would aggravate under employment, and adversely impact poorer states.

Panel Discussion

In the panel discussion question was raised – Predictions are being made that since demonetization the cash component in the construction sector would reduce due to liquidity crunch, resulting in land getting cheaper, and rise in the number of joint ventures and deals taking place. Have the panelists observed this happening?

On this the panelists concluded:

- Little to no impact on land prices, but prices of apartments have gone down, input credit and transferring the benefits of GST, could be one of the reasons for this. Another reason can be push from the developers to sell the unsold inventory in the market.

- Number of Joint ventures have increased and as the market becomes more mature, developers would prefer to have less capital invested in a particular project and further more joint venture deals would flourish.

Other panelists were of the view that one impact of demonetization is that more bank accounts have been opened for the laborers and other staff working on construction sites and thus some formalization has been achieved. Compliance on labor payment front has seen a rise and wages from now onwards are being more fairly paid.

Another important point that was raised in the discussion was that as the construction industry becomes more organized and more regularization is brought in the built environment sector, this would bring more inflationary pressure resulting prices of real estate to rise and people and government should be ready to accept this fact.

When the question was raised weather these policy reforms have any impact on large city level urban projects the panel conclude that the slowing down of economy by GST and demonetization would impact the planned urbanization of cities. The experts argued that if the activities which make a place urban are affected this would impact planned urbanization. The government to maintain the fiscal deficit could cut back on the funding of Infrastructure and social housing projects, adversely affecting such projects.

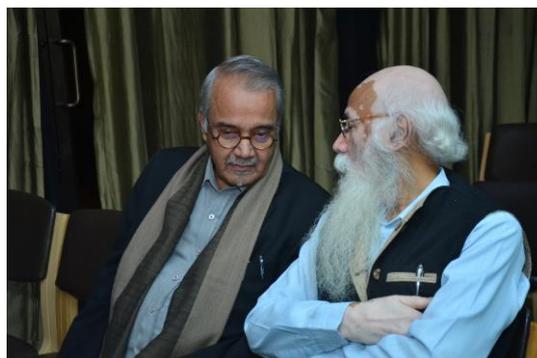


Some positives impacts that were noted are - Since demonetization a increase in the tax compliance has been noticed but the share is very small and how much of this would actually translate in the increase of tax collection will have to be seen. The panelists all agreed that such policy changes indicate that these are the signs of a paradigm shift towards a greater regulated and greater compliance driven country. This is a huge positive impact, as people have started thinking in terms of compliance.

As per the panelists to improve the economic condition of the country, investments have to be revived. For this capacity utilization of the country needs to improve. Public sector could facilitate the improving of capacity utilization.

On discussing GST, the important points raised in the discussion were:

- ***GST on long leases of land is a very negative move. RICS will raise this point with the appropriate authorities and hope fully it will be removed. Long leases should be treated as sales and should be exempted from the tax net.***
- In the present GST structure Input credit can't be taken when properties are let-out in REIT's, this should also be changed and Lease should not be treated as a service. This is one of the reasons which have pushed back REIT's in India.
- ***The expert panelists were in unison that whole of Real Estate should be brought under GST. Stamp duty should be removed and some other financing mechanism of local bodies should be devised.***
- It was also concluded that instead of blaming the real estate sector of avoiding taxes, government should start using the collected funds under labor cess, which everyone pays for labor welfare, but are lying unutilized. On a country level this is a more than 30 billion USD.
- Government should work towards making things simple, things like tax matching, will make things very difficult for the built environment industry.
- Expecting further decrease in the real estate prices was not realistic and the industry believes as the unsold inventory will decrease, sentiments will improve because there is a rising demand for real estate in the country.
- The artificial scarcity of land that our master plans create by fixing the land use should be corrected as high land prices is the main cause of high property prices and if real estate prices are to be reduced, factors affecting land prices should be looked into.
- If the government really wants the housing for all to succeed, and give a real push to affordable housing, it should remove the 32 taxes presently levied on it.





The final conclusion were:

- All expert panelists agreed that the intention of the government was good in taking these measures but if not implemented properly it would create more problems than solutions.
- Inefficiencies in implementation of government policies should not be tolerated, as this creates a trust deficit between the industry and government.
- Government should bring all remaining sectors under GST to remove the cascading effect, tax rates should be lowered further.
- Reverse charge and input tax credit should be removed, especially for the unorganized sector. GST is regressive in its present form. We need to keep taxes simple and need to move towards compliance in collection of taxes. This would further help in reducing rates under GST, which should ideally have a two slab system and rates below 10%.
- The panelist agreed and appreciated that the government is listening to the industry and making the required changes. They also felt that the built environment sector though presents rational arguments to the government, the government has so far not delivered to the desired level.
- Now that many reforms have been brought in, it's time to improve the investment climate in the country.