Other side of 'bayana'

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IT IS A general practice to make a token payment towards an agreement to sell, referred to as '*bayana*' which is forfeited/payable as per the terms of the agreement if any of the parties to the agreement fails to honour the commitment. What complications can it cause to the calculation of capital gain under the Income Tax Act 1961 has to be seen.

Let us consider a few hypothetical situations:

What happens if a person agrees to sell a residential house and gives advance money(bayana) of Rs.1,00,000 and later,as per agreement, the bayana is forefeited ?

The amount so forfeited shall go to reduce the cost of acquisition of the asset and the receipt will not lead to any tax liability as the asset cost will be reduced by the advance money forfeited .

If the vendor commits a default and the vendee receives some compensation besides the refund of the earnest money paid by him, such compensation shall be subject to capital gains as it will amount to relinquishment of a right by the vendee..

What happens if the advance money was towards purchase of an office building, can it be treated as a business expenditure in the hands of the supposedly purchaser?

The amount cannot be claimed as revenue expenditure, because it has been held in CIT *v. Jaipur Mineral Develop Syndicate (1995) 216 ITR 469 (Raj)*, that where the payment is towards a capital asset the amount lost upon forfeiture will not be revenue loss though the sum may not have the same consequence or character in the hands of the recipient or beneficiary.

How will the indexation of the asset be done in the hands of the owner, in case of future sale?

The original cost of acquisition will be indexed upto the year of forfeiture of advance money and out of it the amount of advance money forfeited shall be reduced. Then again this value shall be indexed upto the year of sale in order to compute the indexed cost of acquisition. This indexed cost of acquisition shall then be deducted out of the total sale proceeds to compute the taxable capital gains.

Opinion : Though a plain reading of section 51 would mean otherwise, I am of the firm opinion that indexation has been brought in with the intention to talk in the terms of present value of money involved in the transaction; therefore it shall not be expected to reduce the actual cost of acquisition by the forfeited amount and then to index it.

Other points to be kept in mind

(i) For purposes of section 51 , no distinction is made between moneys received and retained by way of 'advance' and 'other money'. The phrase 'other money' would cover deposits made by the purchaser for guaranteeing due performance of the contracts and not forming part of the consideration.

(ii) Only when the advance or the other money has been a)received ,and b)retained or forfeited by the assessee , then only it has to be deducted from the cost of the asset. If such an advance was received and retained by any previous owner, the same shall not be deducted from the cost of the asset.

(iii) If the advance money forfeited was received by the assessee before 1.4.1981 and the assessee has assumed the F.M.V of the asset as on 1.4.1981 as the cost of acquisition, such advance money received (though before 1.4.1981) shall also be deducted as in the section it is written that it will be deducted from the fair market value.

(iv) A situation may arise where advance money forfeited is more than the cost of 'acquisition'.In such a case, the excess of the advance money forfeited over the cost of 'acquisition' of such asset shall not be taxable in the previous year in which advance money is forfeited as there is no transfer. However, such excess may be taxable as capital gain in the previous year in which such asset is actually sold either to such party or any other party .Ref: CIT v Sterling & Investment Corporation Ltd.,(1980) 123 ITR 441 (BOM)