

## Should you sell an under-construction Property now because the price is great, or wait until the Property is completed to avail LTCG?

**For Indians, real estate investment is an emotionally intensive decision. But buying it will significantly impact our Cash Flows.** While investing in a property, an investor is in perpetual confusion about whether to invest in a ready-to-move-in property or an under-construction one. While a ready property allows for immediate possession, an under-construction property lets you take control at a later stage and deposit the finances accordingly.

Recently, one of our clients had come up with a question to **Dilzer Consultants Pvt Ltd.** stating he had bought an under-construction apartment almost one and a half years back. The purchase price of the apartment then was Rs.3,12,00,000 inclusive of all charges. He made a down payment of approx. 30% from his side, and for the rest of the money, around Rs.2,00,50,000, a loan was taken. The loan amount of Rs.1,82,83,975 was disbursed, and the client is paying an equivalent EMI. As of 21 Aug 2022, he has paid 17 EMI, which amounts to Rs.30,60,000. The outstanding loan amount as of 21 August 2022 is Rs.1,64,91,925.

Recently the builder gave him an offer to **buy back the apartment** for a price of Rs.3,50,00,000. With this data in hand, our client approached us to decide if selling the Property now is beneficial or if he should wait and sell the Property once the construction is completed.

*In this scenario, we considered the impact of capital gain tax and interest paid along with all other expenses in the calculation and the opportunity cost of this investment.*

Before taking you through the calculation, let's understand some intricacies in selling an under-construction property. Many people have this question in mind

### **“Is it Legal to sell an under-construction property?”**

Yes, it is Legal. Many investors try out what is usually called “flipping the property”. They enter the property market and exit it to make some profit on it. Skilled Investors will usually do it. However, if you haven't taken possession yet, there are some factors you (assigner) need to mind.

### **“The Agreement”**

If you haven't taken possession of the flat, the builder will be a party to your agreement for the transaction with the potential buyer of your unit. This is known as Assignment Deal which is a tripartite agreement between the assigner (you), assignee (potential buyer), and the builder. This is important because, as the first home buyer and now the seller, we haven't fulfilled the commitment of paying the full amount to the developer nor do we have complete rights over the Property as we don't possess the full house yet.

### **“The Cost of the Deal”**

We may be a seller (Assigner) however, we are a buyer in the first place. We should ensure that the assignee (Potential Buyer) to whom we will sell our new unit can pay us. If he/she has simply given us some token money and is taking a long time to pay us the remaining amount, then we may be in trouble especially if the deal gets canceled.

### **“The Mortgage”**

We need to check if the assignee (Potential Buyer) is eligible to take a loan. Do remember there are a bunch of reasons a loan may get rejected. So never fall for a word-of-mouth assurance from the assignee (Potential Buyer).

### **“The Terms of Payment”**

We need to check if the assignee (Potential Buyer) is willing to close or take over our loan. In most cases, an assignee would want to take over and close the loan that the seller is paying however; banks usually are not comfortable with this arrangement.

Remember that the property title is still with the builder, and a conditional no-objection certificate is therefore necessary. Experts say that two loans taken on one Property by the assigner and the assignee is a tricky situation.

You should seek help from your Mortgage / financial adviser.

### **“What if Deal Fails?”**

If the new buyer backs out, the builder may or may not choose to return the transfer fee paid by the assigner to the builder. The best way would be to request the builder to hold on to the fee till you find a new buyer.

Now let's get into the calculation part. With all the input data in hand, we consider 2 scenarios.

- **Selling the Under-Construction Property Now (STCG).**
- **Wait until the Property is completed (Feb 2023-LTCG).**

## Scenario 1:

As mentioned earlier, the Sale Consideration of the Property is Rs.3,50,00,000.

The price at which they bought the Property inclusive of all the charges was Rs.3,12,00,000.

The difference between the Sale Price & the Purchase Price will be our capital gain/loss which is a gain of Rs.38,00,000 in this case.

For a real estate property, which is under construction if the holding period is less than 36 months it is subjected to Short Term capital gains, and taxation is subjected as per income tax slabs.

Since the holding period is less than 36 months and the client falls under the 30% tax slab, the taxation, in this case, will be Short Term Capital Gains which is around Rs.11,40,000.

Considering all the expenses, interest payout and tax, the Net gain for the client in this scenario would be Rs.26,60,000.

Scenario 1_Selling the Property Now	
Sale Price	3,50,00,000
Price Agreed Upon with Builder	3,12,00,000
<b>Capital Gain</b>	<b>38,00,000</b>
Capital Gain Tax @30%	<b>11,40,000</b>
<b>Net Sale Proceeds</b>	<b>3,38,60,000</b>
Loan Disbursement	1,82,83,975
Self Contribution	1,29,16,025
Capital Gain Tax	11,40,000
Total Payment	3,23,40,000
<b>Net Gain</b>	<b>26,60,000</b>

## Scenario 2:

For a constructed real estate property, if the holding period is less than 24 months, the Property is subjected to short-term capital gains and taxation will be as per income tax slabs.

In case of a holding period greater than 24 months, we consider this as Long term Capital Gains and taxation will be 20% along with Indexation benefits.

So, in this scenario, if we wait until February 2023, the Property will be fully constructed and the taxes would be long-term capital gain.

We will consider a 5% indexation benefit on the property purchase price, which is Rs.3,27,60,000.

The difference between the Sale Price & the Indexed cost of the purchase price will be our capital gain/loss, which is a gain of Rs.22,40,000.

So, the holding period would be greater than 24 months, and the taxation, in this case, will be long-term capital gains, which is around Rs.4,48,000.

Apart from all the expenses, interest payout, and tax we should also consider EMI's paid out until February 2023. The Net gain for the client in this scenario would be Rs.21,13,000.

Scenario 2_Wait until the Property is completed (Feb 23)	
Sale Price	3,50,00,000
Price Agreed Upon with Builder	3,12,00,000
Indexed Cost of Acquisition @5%	3,27,60,000
Capital Gain	22,40,000
<b>Capital Gain Tax @20%</b>	<b>4,48,000</b>
Additional EMI to be Paid from Aug 22 to Feb 23	12,39,000
<b>Net Sale Proceeds</b>	<b>3,33,13,000</b>
Loan Disbursement	1,82,83,975
Self-Contribution	1,29,16,025

Capital Gain Tax	4,48,000
Additional EMI to be Paid	12,39,000
Total Payment	3,28,87,000
<b>Net Gain</b>	<b>21,13,000</b>

Comparing both scenarios, we can see that selling the under-construction Property with STCG would be a better option. In a current increasing interest rate economy, the home loan interest would again add a burden to the loan component for the upcoming few months. Keeping all this in mind disposing of the Property now would be advisable.

Adding a bonus point to the case study, If there is no need for the funds until February 2023 (i.e. next 7 months), clients can invest the proceeds from the sale after paying the taxes into bank fixed deposits or short-term debt funds which will yield an extra return of Rs.3,22,013 post-tax returns. The calculation for the same can be seen below.

<b>Selling Property now &amp; investing the proceeds for 7 month</b>	
Investment amount in short term funds	1,55,76,025
Rate of Return - Expected	5%
Estimated Value by Feb 23	<b>1,60,36,044</b>
Capital Gain	<b>4,60,019</b>
Capital Gain Tax @30%	<b>1,38,006</b>
Net Proceeds by end of Feb 23	29,82,013

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