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# Taxability of Security Deposits under Joint Development Agreements: Why Capital Gains Should Arise only on “Transfer” through Possession

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**ABSTRACT:** Joint Development Agreements (JDAs) have become a common mechanism for real estate development in India, enabling landowners and developers to collaborate without outright land sale. However, these arrangements often create uncertainty regarding the timing of capital gains taxation under the Income Tax Act, 1961. A key issue arises when landowners receive an interest-free refundable security deposit from developers whether such receipts should be treated as consideration triggering capital gains tax.

This paper examines the legal position through doctrinal analysis of statutory provisions and judicial interpretation, with particular focus on the Hyderabad Income Tax Appellate Tribunal ruling in DCIT v. Nagam Suguna (2022). The tribunal held that a ₹7 crore refundable security deposit received under a Joint Development Agreement did not attract capital gains tax because legal possession of the land had not been transferred as required under Section 2(47)(v) of the Income Tax Act read with Section 53A of the Transfer of Property Act, 1882. The study analyses the distinction between refundable deposits and real consideration, as well as the difference between permissive access and legal possession.

The findings highlight that capital gains taxation should arise only when there is an actual transfer of control and economic benefit. Such an interpretation prevents premature taxation, protects taxpayer liquidity, and improves certainty in real estate transactions.

The study examines when a “transfer” occurs in Joint Development Agreements under Section 2(47)(v) of the Income Tax Act, 1961 read with Section 53A of the Transfer of Property Act, 1882. It focuses on whether an interest-free refundable security deposit received from a developer can be treated as consideration that triggers capital gains taxation. The research analyses the ruling in DCIT v. Nagam Suguna to understand the judicial approach to such arrangements. It aims to distinguish refundable deposits from actual consideration and permissive access from legal possession to reduce premature taxation in JDA transactions.

**KEYWORDS:** Joint Development Agreement (JDA), Capital Gains, Section 2(47)(v), Section 53A TPA, Refundable Security Deposit, Possession, Section 45(5A), Real Income Theory, ITAT.

## I. INTRODUCTION

Over the past two decades, Joint Development Agreements (JDAs) have become a preferred structure for real estate development in India. They allow landowners to unlock the value of their property without selling it outright, while developers gain access to land without making large upfront purchases.

Under Section 45 of the Income Tax Act, 1961, capital gains arise only upon “transfer” of a capital asset (Income Tax Act, 1961). However, Section 2(47)(v) expands the definition of transfer to include transactions involving possession in part performance under Section 53A of the Transfer of Property Act, 1882 (Transfer of Property Act, 1882). This expanded definition has become central to disputes in JDA taxation.



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In practice, tax authorities often argue that once a JDA is executed and money is received, a transfer has effectively occurred. However, judicial interpretation has clarified that permissive possession does not automatically amount to possession under Section 53A (AZB & Partners, 2022).

The Hyderabad ITAT ruling in *DCIT v. Nagam Suguna* (2022) directly addressed this issue. The tribunal held that ₹7 crore received under the JDA was an interest-free refundable security deposit and not taxable in the absence of legal possession transfer. This interpretation aligns with the broader real income principle, which requires taxation to correspond with actual realization of economic benefit (Auerbach, 1988; Cavalcante Koury, 2023).

From a policy perspective, premature taxation may create liquidity stress and distort redevelopment incentives (Yamazaki, 1996). The introduction of Section 45(5A) reflects legislative intent to align taxation timing with economic crystallization (Income Tax Act, 1961; Income Tax Department, n.d.).

### Problem Statement

In JDA transactions, tax disputes frequently arise because tax authorities may treat **execution of the agreement and receipt of money** as sufficient to conclude that a “transfer” has occurred, even when the payment is a **refundable security deposit** and the landowner has not handed over **legal possession** in the manner required under Section 2(47)(v) read with Section 53A of the Transfer of Property Act. This leads to premature capital gains taxation, liquidity hardship, and avoidable litigation, making it necessary to develop a clear, evidence-based framework to distinguish refundable deposits from consideration and permissive access from possession for tax purposes.

This study aims to examine how “transfer” is determined in Joint Development Agreements under Section 2(47)(v) of the Income Tax Act read with Section 53A of the Transfer of Property Act, and to analyse whether receipt of an interest-free refundable security deposit can be treated as consideration triggering capital gains. The paper further seeks to interpret the Hyderabad ITAT ruling in *DCIT v. Nagma Suguna* and derive practical compliance principles that reduce premature taxation and litigation in JDA transactions.

## II. REVIEW OF LITERATURE

(Y. Kanemoto 1996) If the tax basis of an asset is sufficiently high, the taxable capital gain will be minimal or zero. Consequently, investors will incur little or no tax liability on sale or transfer, thereby eliminating any incentive to defer transactions and thus the lock-in effect.

(Fukuju Yamazaki 1996) The taxation of capital gains could act as a deterrent to the sale and redevelopment of land, as it may increase the cost of transactions, resulting in inefficient land use. However, the effect of the taxation system on land use is theoretically ambiguous.

(Nigam Nuggehally International Taxation 2019) The source explains India’s liberal approach to sourcing capital gains, emphasizing the situs of assets as the primary determining factor for taxability. However, it does not specifically analyze issues related to security deposits or capital gains arising from joint development agreements.

(Alan J. Auerbach 1988) The proposed method of taxing capital gains eliminates the deferral advantage by providing for the imposition of interest on the accumulated gains at the time of realization. Nevertheless, it does not specifically consider the treatment of security deposits, joint development agreements, or transfers made through possession.

(Jeffrey L. Kwall 2010) The realization requirement in the U.S. system causes inequity and inefficiency by permitting the appreciation of assets to be taxed at a later date compared to other income. The proposed standard of disposition will tax gains at the time of transfer, without even taking consideration into account, providing a better alternative to the complicated mark-to-market systems.

(A. Dugar, L. Bhandari Asia-Pacific Tax Bulletin 2018) However, capital gains that result from the transfer of indirect shares may not be taxable in India, depending on certain domestic laws and tax treaties. These laws may limit the taxing rights of India, particularly if the shares are valued based on foreign entities rather than assets in India.



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(S.P. Singh, S. Goyal, A. (. Kumar Asia-Pacific Tax Bulletin 2010 )The article discusses tax challenges in the context of turnkey projects in India, focusing on income characterization and taxability. Nevertheless, it does not address the treatment of security deposits or the tax implications of joint development agreements.

(A. Dugar, L. Bhandari Asia-Pacific Tax Bulletin 2018) Capital gains arising from share transfers are liable to tax in India if the transferring shareholder is not the beneficial owner of the shares. The beneficial ownership of shares is determined by analyzing the legal documents, control, and board/shareholder meeting minutes.

(B. Savero Bulletin for International Taxation 2018) The source discusses how China and India tax indirect transfers of assets to avoid erosion of their tax bases. Although it embodies the tenets of taxing capital gains on effective transfer, it does not specifically deal with security deposits and joint development agreements.

(P.A. Cavalcante Koury Bulletin for International Taxation 2023) The right to freedom sustains the taxation of capital gains on a realization basis as it upholds individual freedom over property. The taxation of gains only when they are transferred through possession ensures that liability is triggered only when control and economic benefit actually change.

### III. METHODOLOGY

#### 3.1 Type of Study:

Doctrinal and analytical legal research (qualitative), supported by comparative case-pattern review.

#### Sample / Case Selection:

Primary focus on the Hyderabad ITAT ruling reported as **DCIT v. Nagam Suguna [2022] 135 taxmann.com 198 (Hyderabad – Trib.)**, which directly addresses whether ₹7 crore received under a JDA (as refundable security deposit) triggers capital gains without possession transfer. To strengthen interpretation, the study also references related tribunal/case discussions on “permissive possession” and Section 53A applicability in development agreements, as available through legal databases and professional commentary.

#### 3.2 Data Sources:

1. **Statutory law:** Income Tax Act, 1961 (Section 45, Section 2(47)); Transfer of Property Act, 1882 (Section 53A).
2. **Government sources:** Income Tax Department learning material on Joint Development Agreements, including treatment under Section 45(5A).
3. **Case reports / summaries:** Case digest/reporting of the Hyderabad ITAT decision and related commentary.
4. **Secondary sources:** Explanatory materials on JDA taxation timing and practice notes.

#### 3.3 Analysis Technique:

- **Issue–Rule–Application–Conclusion (IRAC):** identifying the taxable event, applying the “transfer” test under Section 2(47)(v) r/w Section 53A, and evaluating the character of receipt (deposit vs consideration).
- **Document-based indicators:** examining contractual terms (refundable nature, linkage to performance, possession clause, rights granted) and factual timing (possession actually handed over or not in the relevant year).
- **Interpretive synthesis:** deriving practical principles and recommendations from the tribunal’s reasoning and aligning them with broader JDA tax policy reflected in government guidance.

### IV. ANALYSIS AND INTERPRETATION

#### 4.1 Core legal test: When does a JDA become a “transfer”?

For capital gains, the key trigger is “transfer.” In JDAs, tax authorities often invoke Section 2(47)(v), which depends on possession being given in a Section 53A (TPA) sense. This requires more than mere contractual intention; it requires that the developer’s possession is of the nature that supports part performance i.e., the developer’s rights are sufficiently substantial and the landowner’s control is effectively reduced.



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Tribunal reasoning across similar disputes shows a consistent approach: if the developer has only **permissive possession** (access for development) rather than legal possession, Section 53A may not apply, and therefore Section 2(47)(v) should not be triggered.

### 4.2 Character of receipt: refundable security deposit is not “consideration”

In the focal case, ₹7 crore was treated by the AO as long-term capital gains consideration. The tribunal emphasized that the amount was **interest-free refundable security deposit** meant to ensure completion, not a final consideration for transfer.

This matters because consideration typically represents price for transfer non-refundable, linked to sale/exchange of rights. A refundable security deposit is economically closer to a performance guarantee; taxing it as capital gains can create tax on an amount that may be returned and on a transfer that has not happened.

### 4.3 Application to the facts: no possession + no real consideration = no capital gains in that year

The tribunal’s conclusion follows a simple logic:

- The assessee contributed land for development; capital gains (if any) are more appropriately linked to later events such as sale of the developed share.
- The ₹7 crore receipt was refundable deposit, not consideration.
- Possession was not vested with the developer in the relevant year; therefore, Section 2(47)(v) was not attracted.

**Interpretation:** The ruling supports a compliance principle: **JDA’s should not be taxed merely on signing or deposit receipt—tax timing must follow the statutory “transfer” trigger, especially possession.**

## V. DISCUSSION: CONTRIBUTION TO SOCIETY

This interpretation contributes to society in practical, measurable ways. First, it promotes **fairness and liquidity protection** for landowners. Real estate development is long cycle; if tax is imposed before the landowner receives actual, non-refundable gains or saleable developed property, taxpayers can face severe cash-flow problems and may be forced into distress borrowing or sale. Recognizing that refundable security deposits are not immediate taxable consideration prevents such hardship.

Second, it encourages **voluntary tax compliance** and reduces litigation. When tax demands appear premature or disconnected from economic reality, taxpayers are more likely to dispute assessments, leading to prolonged litigation and administrative burden. A clear rule no taxation until possession transfer/real consideration improves predictability and reduces unnecessary disputes, saving time for both taxpayers and the tax department.

Third, it supports **healthier real estate development outcomes**. JDAs enable redevelopment, housing supply, and infrastructure-linked growth. If tax uncertainty discourages JDAs or makes them legally risky, projects may slow down, indirectly affecting employment in construction and allied industries. A consistent interpretive framework reduces friction in legitimate development activity without compromising future taxation because gains can still be taxed when transfer occurs or when developed shares are sold.

Finally, it aligns taxation more closely with the principle that tax should apply to **real income and real transfer**, not refundable security mechanisms. By focusing on possession and the true nature of receipts, the approach improves the integrity and credibility of the tax system, which benefits society through better governance and smoother economic transactions.

## VI. CONCLUSION

Joint Development Agreements have become an important model for real estate development in India, but they also raise complex tax timing issues. One of the most significant disputes relates to whether payments received by landowners at the time of signing a development agreement should trigger capital gains taxation. The analysis of statutory provisions and the Hyderabad ITAT ruling in DCIT v. Nagam Suguna (2022) demonstrates that capital gains should arise only when a legally recognized “transfer” takes place.



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The tribunal's decision clarifies that a refundable security deposit cannot automatically be treated as consideration for transfer. Unless possession is transferred in the legal sense contemplated under Section 53A of the Transfer of Property Act, the transaction cannot fall within Section 2(47)(v) of the Income Tax Act. Therefore, merely executing a Joint Development Agreement or receiving a deposit does not constitute a taxable transfer.

This interpretation strengthens the principle that taxation must correspond with real economic gain. By aligning tax liability with actual transfer of control and benefit, the ruling helps prevent premature taxation, reduces liquidity pressure on landowners, and enhances predictability in real estate transactions.

The present study focuses primarily on doctrinal legal analysis and the interpretation of a specific tribunal ruling related to Joint Development Agreements. Future research can expand this work by conducting empirical studies on multiple JDA-related tax disputes across various tribunals and courts in India to identify broader judicial trends. Additionally, further research may examine how Section 45(5A) interacts with possession-based transfer provisions in different factual situations. Another potential area of study is the development of standardized contractual frameworks for JDAs that clearly define possession rights and payment structures in order to reduce tax ambiguity. Such extended research could contribute to improved policy formulation and more efficient tax compliance in the real estate sector.

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