FIDC

Finance Industry Development Council

(A body incorporated as a Self Regulatory Organization for Registered NBFCs)

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June 17, 2017

Shri Upender Gupta
Commissioner, GST
The Working Group for GST
(Banking & Financial Services)
New Delhi

Respected Sir,

Re: **Proposed GST Regime - Concerns of the NBFC Sector**

Finance Industry Development Council (FIDC) is a Self-Regulatory Organization (SRO) cum Representative Body of the NBFCs, registered with the Reserve Bank of India. FIDC was formed 12 years ago, and is the recognized face of NBFCs, especially, those engaged in asset financing. We have been engaged in regular interactions both with Reserve Bank of India and Govt. of India, which include pre-budget meetings and also important policy related meetings with RBI. Almost all the leading NBFCs and a large number of small and medium sized NBFCs are our members.

We hereby submit our key concerns regarding the proposed GST regime, and our suggestions thereon :

1. Leasing Needs to be Promoted for Financing of MSMEs and Farm Sector- Need for 100% Input Tax Credit & Lowest GST Rate on Lease Rentals

Under the current VAT regime, 100% ITC is available when goods/assets are purchased by NBFCs for furtherance of its business i.e., by way of Transfer of right to use (Leasing) and delivery under hire purchase system. Under the proposed GST, both Financial and Operating Lease are to be considered as "supply of service". In the event of an NBFC deciding to opt and go in for 50% ITC (as per Sec.17(4) of the CGST Bill), then in such case, it will be deprived of 100% ITC which it had under the VAT regime.

Similarly, in such Leasing/hire purchase transactions, if the rate of tax for supply of goods and supply of services differs, it will create unnecessary confusion and may lead to litigation.

World over, "Leasing" has been the most suitable tool and has been effectively used for :

1. Financing MSMEs, including Start-ups, by addressing their need for capital investment required for acquisition of assets like equipment, machinery etc.
2. Enabling farmers to use the right equipment without making any capital investment
3. Making capital Investment in the equipment to be used to build Infrastructure

International Finance Corporation (IFC) report on "Leasing in Development" talks about how leasing has played a key role in the development of MSME and Farm sectors in the emerging economies of Uzbekistan, Ravanda,Yemen, Tanzania and many other countries. Unfortunately, leasing has suffered in India due to imprudent taxation policies primarily due to dual / multiple taxation.

Suggestion:

There is a crying need to promote leasing of movable assets. For this:

i) *Following para needs to be inserted in Rule 3- Claim of Credit by the Banking Company or Financial Institution of the ITC Rule:*
"The said company or institution shall avail 100% ITC on tax paid on purchase of goods given on lease/ hire purchase".

ii) *to put the Lease Rentals in the lowest rate category of 5%. However, the same may not apply to lease rentals on luxury goods*

iii) *The existing lease transactions have already suffered Central Excise and VAT, apart from Service Tax (for the service element on a notional value). Hence for all such existing transactions, instead of applying the proposed GST rate applicable on "supply of goods", a lower rate of GST , on the value-added portion under hire purchase / lease rentals can be considered. Similar lower rate can be considered when the Asset is sold at the end/termination of the contract, under such existing transactions.*

2. **Penal interest/charges for delayed remittance of EMI should be Exempted**

Under the list of exemptions decided by the GST council, the services by way of extending loans or advances in so far as the consideration is represented by way of interest or discount continues to be exempt. The assets are funded out of borrowed funds and any late realisation of monthly instalments would result in erosion in net earnings. To protect such erosion in earnings, additional interest/additional finance charges for such delayed remittance is charged from the due date of instalment till the date of actual realisation.

Value of Taxable supply under Sec.15 (2)(d) of the GST Act includes interest or late fee or penalty for delayed payment of any consideration for any supply. Whereas under the current Service Tax provisions (Rule-6(2)(iv) of the Service Tax (Determination of Value Rules), 2006), penal Interest/Charges charged for delayed remittance of EMI is excluded.

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Suggestion:

Since both interest and additional interest/charges for delayed remittance are similar in nature, we request you to exclude the penal interest/charges for delayed payment of the instalments from the value of taxable supply under GST. The same is already exempted from the levy of service tax.

3. Sale of Repossessed Assets Should Be Exempted

If a borrower commits default in case of asset backed financing, the asset is repossessed by the Financier (Bank/NBFC) and after giving sufficient opportunities, if the default continues, such Financier sells the asset and appropriates the sale proceeds towards the account of the borrower. In this scenario, there won't be any value addition and only value dilution, as the asset is depreciated.

As such, the asset is never reflected in the books of NBFCs, and NBFCs merely facilitate sale on behalf of the defaulting borrower to recover our dues and settle his account. Further, the input at the time of purchase would not have been utilised by the customer. So, in case of any levy of GST on sale of repossessed assets, No ITC shall be possible as the asset is owned by the defaulting borrower and the invoice of the asset is also with the borrower.

In a scenario, where banks and financial institutions are grappling with the menace of NPAs, repossession and subsequent sale of repossessed assets, is an important tool to fight this menace.

Suggestion:

Sale of assets repossessed in case of default (ITC not utilised cases) should be exempt from the levy of GST.

4. Assignment of Receivables Need to be Exempted

The CGST Bill exempts "Actionable Claims" from the levy of GST. The definition of actionable claims under the CGST bill has been derived from the Transfer of Property Act, 1882. As per this definition, assignment of receivables secured by hypothecation or pledge of movable assets are not treated as actionable claims. As such, as per the prevailing provisions , assignment of receivables falls under the definition of "supply" and shall be subject to the levy of GST.

Assignments of receivables are effectively used for securitization. They act as a very important mode of refinancing for NBFCs. Bilateral assignment of receivables by NBFCs to banks, especially, in retail lending not only provides funding to NBFCs but adds tremendous value to the asset book of the banks. Both RBI and SEBI have been working to create an enabling environment for such transactions.

Suggestion:

We therefore request that assignment of receivables secured by hypothecation or pledge of movable assets should be exempted from the levy of GST.

We hope that our above said concerns shall be given a favorable consideration, as they shall also have the potential to affect the development of important sectors like MSMEs, Small Road Transport Operators , Agriculture and Infrastructure.

We take this opportunity to request you to kindly give us an opportunity to meet and discuss the above concerns in detail.

Thanking you in anticipation

Warm Regards
For **Finance Industry Development Council**

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