



Date: 29th March, 2017

To,
Shri Upender Gupta
Commissioner
Goods & Service Tax Policy Wing,
Department of Revenue,
Central Board of Excise & Customs,
Government of India,
North Block
New Delhi – 110 001

Sub: Representation on concerns of the Asset Finance Industry on Goods and Service Tax law

Dear Sir,

Asset Finance Association of India (AFAI), an industry body formed with the objective of promoting leasing, factoring and other asset-backed financing entities is an initiative by the Indian Securitisation Foundation (ISF), a non-profit organization incorporated with the cause of promoting capital market instruments in the country. Some of the eminent players of the leasing industry are members to AFAI and are dedicated to the cause of promoting leasing in India. The details of AFAI, its activities and members are provided for in **Annexure I** to this representation.

As representative body for the leasing industry we wanted to bring to fore certain concerns in the Central Goods and Services Tax Bill, 2017 (“CGST Bill”) and its impact on the leasing industry in the present form in this representation.

Summary of the Representation

- The banking and financial services in common parlance have always included activities like lending, depositing, issuing of pay order, demand draft, cheque, letter of credit and bill of exchange, financial leasing services including equipment leasing and hire-purchase, etc under its ambit. The reason being financial leasing and hire purchase transactions in substance partakes the character of loans and advances as these involve grant of assets to lessors / hire purchasers on credit terms and at predetermined rentals.
- Section 65(12)¹ of the Finance Act 1994 also included financial leasing and hire purchase transaction under the scope of banking and financial services. So including financial leasing and hire purchase transaction under financial services is justifiable. However in the CGST Bill there is no reference of banking and financial services.

¹<http://www.cbec.gov.in/resources/htdocs-servicetax/st-act-ason24oct2013.pdf;jsessionid=36AC9D5AEFA553EED81E3527914D64C4>



- In the existing law, loan transactions forming part of the banking and financial services are exempt from applicability of service tax on the interest component. Financial leases and hire purchase while being forms of asset-backed lending are in substance financial transactions and therefore they should be on the equal footing as loans.
- There have been several judicial pronouncements where it has been substantiated that financial leases are akin to loan. In the case of **Association of leasing and financial services company v/s Union of India**, paragraph 20 and 21 of the judgment clearly brings out the fact that financial leasing and hire purchase transactions are a mode of long term funding. In case of **Asea Brown Baveri Ltd v/s Industrial Finance Corporation of India**, the judgment brings fore the fact that financial lease is nothing but loans in disguise.
- Considering the fact that financial leases, hire purchase and loans are in substance financial transactions, there should be tax parity provided for the financial products to have a level playing field. Presently a financial lease is subject to sales tax and service tax both while loans are exempt from applicability of service tax. A level playing field on the tax perspective will allow the market to decide on the financial product that may be suitable for them.
- In light of the above discussion we request you to consider providing similar treatment to loans, financial leases and hire purchase transactions from applicability of indirect taxation perspective for the tax laws to facilitate level playing field for all the three products. It will enable leasing to grow in India and will be a viable alternate to loans.

We will be highly obliged if the leasing and hire purchase transactions are included within the scope of financial services and the treatment as would be available to interest on loans, deposits and advances is extended to the interest component in specified transaction under the CGST Bill.

Leasing Industry in India

The Indian leasing industry has witnessed some growth in leasing volumes since 2010 and has seen several new players venture into new asset classes after leasing in India came to a sudden halt in 1996. Leasing has found favour as some of the issues from the past resolved, corporates preferred usage of several assets over ownership, technological obsolescence also created an inclination towards appreciating usage benefits over ownership, leasing facilitated creation of new customer class, as a tool to boost sales for some asset classes and more.

While assessing the performance of the Indian leasing industry, it is noted that the leasing volumes stood at around USD 669 million² during FY 2014-2015 as opposed to USD 505 million during FY 2013-2014. The leasing industry outlines the upward trajectory motion in terms of growth. The acquisition of capital goods involve high cash outflow, thus importers

² The leasing volumes do not include new leasing business volumes of Indian Railway Finance Corporation a subsidiary of Indian Railways



opt for equipment leasing rather than buying outright. Leasing, as an alternative provides several benefits which are enumerated below:

1. Technological up gradations are suitably met with the lease form of financing. It is easy for companies to replace their worn out or obsolete machines with the leased assets.
2. Hedging of technological obsolescence helps equipment users to avoid the burdens of ownership, one of them being equipment obsolescence. Much of today's equipment incorporates technology that is rapidly changing.
3. Cash flow constraints make leasing attractive. An outright purchase requires an immediate cash outflow, whereas in case of lease, the cash outflow is spread over years of usage of the asset. Also in case of leased assets, the ownership of the assets is retained by the leasing entity and only the usage of the assets is transferred to the end user. Therefore, in most lease cases, there is no requirement for additional collateral.

The present taxation regime under Service Tax Act

Section 66D of the Finance Act, 1994 (Service Tax Act) provides a list of services that are exempt from the liability of the service tax and is popularly known as “**negative listed services**”.

Clause (i) of sub section (n) of section 66D of the Service Tax Act provides for exemption of the following services:

“services by way of—

- (i) *extending deposits, loans or advances in so far as the consideration is represented by way of interest or discount;”*

From the above clause, it is clear that where the service provider is engaged in providing services of deposits, loans and advances and the consideration for such services are represented by way of interest or discount, then said interest or discount shall be exempted from the liability of the service tax. We understand that the exemption provided in the present service tax regime to interest on loans, advances and deposits will eventually be introduced in the present CGST Bill.

Section **65(12) of the Finance Act 1994** defines banking and financial services and it includes financial leasing and hire purchase transaction within the meaning of financial services. The section has been reproduced below:

XXX

“banking and other financial services” means

- a) *the following services provided by a banking company or a financial institution including a non-banking financial company or any other body corporate or commercial concern, namely :—*



- (i) *financial leasing services including equipment leasing and hire-purchase;*

xxx

The extension of loans and advances constitute financial services to the service receiver. On similar terms, the hire purchase instalments include the interest component on the amount of the assets hired out. The assets hired out represents the amount of loan provided and the interest component included in the said instalments can be said to be consideration for the loans (assets hired by the hirer). While in case of leasing transactions, lessor transfers the right to use the assets to the lessee for fixed periodic rentals. The lease rentals can be construed as interest inclusive instalment for the leased assets. Therefore, both the hire purchase and leasing transactions assumes the character of loan and interest payments.

Proposed taxation Regime under Central Goods and Service Tax Bill, 2017

Section 7 of the CGST Bill states that:

“(1) Supply includes

(a) all forms of supply of goods and/or services such as sale, transfer, barter, exchange, license, rental, lease or disposal made or agreed to be made for a consideration by a person in the course or furtherance of business”

As per the definition of “**supply of goods**” given in section 7, read along with Schedule II, it refers to “**Any transfer of title in goods under an agreement which stipulates that property in goods will pass at a future date upon payment of full consideration as agreed, is a supply of goods**”

A lease transaction usually does not by itself result into a transfer of title. A hire purchase transaction contains an option to buy the asset with the hirer. The above definition of “**transfer of goods**” in Schedule II refers to a transaction resulting into a transfer. Therefore, it seems to cover conditional sales, and not hire purchase contracts.

As per the definition of “**supply of services**” given in Section 7, read with Schedule II, it refers to “**Any transfer of goods or of right in goods or of undivided share in goods without the transfer of title thereof, is a supply of services.**”

On reading the above text it becomes clear that financial lease and hire purchase transaction would be classified under supply of services and therefore would be liable to goods and service tax. This would bring undue hardship on the leasing industry, as presently under the service tax regime tax is chargeable on 10% of the interest component while there is no similar abatement available on the transactions referred above in the CGST Bill.

Our Representation



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We understand the objective with which CGST Bill is being proposed to be implemented in the present complex taxation structure. The seamless movement of the input tax credit and the subsuming of the central and state taxes will eventually bring down the cost of financing the capital goods. As leasing and hire purchase provides the cash flows over a period of time, the levy of GST on interest component would impact the leasing and hire purchase industry as a whole and we think it is quintessential for users of capital goods to have several options for procuring capital assets, other than outright purchase. Leasing and hire purchases are therefore befitting alternatives.

So we humbly request your goodself to kindly consider and facilitate necessary actions to:

- a) classify financial leasing and hire purchase transactions as financial services in the Central Goods and Service Tax Bill, 2017, and
- b) treat interest component on financial leasing and hire purchase transactions at par with interest on loans, deposits and advances in the present CGST Bill.

As AFAI is dedicated to the cause of contributing to the development of the asset backed funding sector in particular, in the event of any further clarification needed, we would be happy to provide the same.

For *Asset Finance Association of India*

SD/-

Abhirup Ghosh



Annexure - I

The Asset Finance Association of India is an initiative by the Indian Securitisation Foundation to bring together the stakeholders of the asset finance sector in India. The organisation is intended to promote, help, develop, protect, encourage and secure, in India, general interest of various forms of asset backed funding by acting as industry association, to organize industry events, forums, discussions to promote research, generally to take care of the interest of trade, industry and commerce, stakeholders, participants and investors in asset finance and generally to act in the best interest of the Indian asset finance sector. Primarily, the asset finance activities to be catered to by the Association include leasing, factoring, trades in receivables, etc.

The Association aims at bringing industry players on a common platform – to join their thoughts, and to provide a voice to their thoughts. The Association aims at providing a strong platform of advocacy for asset finance industry.

Some of the functions of the organisation include:

- **Advocacy:** making representation to various authorities from time to time on matters concerning the following –
 - a. Leasing
 - b. Factoring
 - c. Receivable Financing
 - d. Other forms of asset backed finance.
- **Industry forums and networking:** holding periodic conventions and educational courses.
- **Development of industry standards:** framing self-regulatory standards on disclosures, reporting, servicing reporting, DOs and DONTs for various forms of asset finance.
- **Information exchange:** on matters of common interest, collateral performance etc.

AFAI Executive Committee Members

1. Ms. Simi Thapar

Ms. Simi Thapar is a Head - Equipment Leasing and Financing Solutions - Corporate Finance at Tata Capital. Simi has 25 Years Work Experience in Financial Services across diverse industries and diverse asset and product categories. Ground experience in new business initiative, product development and in devising strategy for organic and inorganic growth of business.



2. Mr. Gautam Munish

Mr. Gautam Munish, currently serving Hewlett Packard financial services as regional sales director is a seasoned finance professional with 20 years of diverse work experience across Asset, Liability and Investment products. He has extensive experience in building and managing business from ground up, with exposure to detailed competitive landscape analysis, compliance and regulatory adherence and evangelizing the merits of a differentiated approach to market.

3. Mr. Sunil Badala

Mr. Sunil Badala is a partner with the financial services tax practice of the Indian Firm of KPMG. He specializes both in domestic corporate tax and international tax and entry and exit strategies for multinationals and large domestic companies investing into/ outside India. He has a total of about 18 years of experience, including 14 years with the India Firm and has extensive experience in International and Domestic taxation, Inbound Entry Strategies for Multinationals and Outbound Structuring Strategies for large domestic companies.

4. Mr. Shrirang Tambe

Mr. Shrirang Tambe founder and CEO of ORIGA Leasing one of the first FinTech asset leasing companies for high growth oriented companies with philosophy of access to finance. His expertise lies in advising and nurturing growth oriented companies across financial and strategic areas.

5. Ms. Nidhi Bothra

Ms. Bothra is a consultant on leasing, asset backed lending, securitisation, structured finance and corporate finance and is Executive Vice President in Vinod Kothari Consultants (P) Ltd. Ms. Bothra has conducted various corporate training workshops on leasing, and has handled several consulting assignments on leasing in different markets. Nidhi has analysed state of leasing industry in several countries and writes the report on the state of leasing industry in India for several years now.

6. Mr. Dipankar Sen

A MBA graduate with specialisation in finance, He has over 20 years of experience in leasing and financial services and today heads the leasing portfolio for Orix in India. His experience has been in both fund based and fee based activities where he has managed the SME, Corporate and PSU segments for their leasing requirements in equipments. Under the leasing portfolio in Orix, he today manages the vehicle leasing business where company offers solutions in both dry and wet leases.