

TAXATION ASPECTS OF NBFCs

ACAЕ VIRTUAL DAY-2 WORKSHOP

KOLKATA

10th MARCH, 2022 - THURSDAY

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SYNOPSIS - I

- Regular provisions
 - S.36(1)(vii) - Bad debts
 - S.36(1)(viia) - Provision for bad debts
 - S.36(1)(viii) - Transfer to special reserve
 - S.43D - Recognition of interest income
 - S.4 & 5 - Interest & gains on bonds
 - S.28 & 45 - SIT v. Investment
 - S.4 & 5 - Interest on NPA
 - S.43B - Deduction on interest expense

SYNOPSIS - II

- Regular provisions
 - S.36(1)(xviii) - M to M losses & S.40A(13) & ICDS VIII
 - S.37(1) – Explanation 1 and penalty
 - S.115 BAA & s.115BAB - Rate of tax
 - S.115JB - MAT
 - S.194LC - TDS on interest on FCB by NBFC
 - S.194LD - TDS on interest on Bonds by NBFC
 - S.14A Disallowance of expenditure
 - S.2(22)(e) - Deemed dividend

SYNOPSIS - III

- Discriminatory provisions
 - S.36(1)(viia) - Provision for bad debts
 - S.36(1)(viii) - Transfer to special reserve
 - S.72A - Set off of losses
 - S.73 - Explanation - Speculation Losses
 - S.80E - Interest on educational loan
 - S.94B - Thin Capitalization
 - S.194A - TDS on interest
 - S.194N - TDS on cash withdrawals
 - S.194P - TDS on Senior citizen

REGULAR PROVISIONS

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BAD DEBTS

s. 36(1)(vii)

- Bad debt allowed as deduction
- Subject to s. 36(2)
 - taxed as income or part before write-off
 - write-off in Books of Account
- Deduction for excess over provision allowed u/s. 36(1)(viia)
- Write-off of NPA as per Prudential Norms
 - Southern Technologies Ltd 320 ITR 577 (SC)
 - Accountancy v. Tax Law
- All assessee including NBFCs

PROVISION FOR BAD DEBTS

s. 36(1)(viiia)

- Deduction for bad debts & doubtful debts
 - Indian banks
 - 8.5% of GTI (before this deduction) + 10% of aggregate rural advances made by rural branches
 - NBFCs, foreign banks, PFI, SFC & SIIC
 - 5% of GTI (before this deduction)
- Not subjected to conditions of s. 36(2)
 - however, 36(2)(v) requires compulsory debit to P & L Account

TRANSFER TO SPECIAL RESERVE

s. 36(1)(viii)

- Deduction allowed to Financial Corporation
 - Engaged in providing long term finance (5 years or more)
- Amount of deduction
 - lower of
 - Actual amount transferred to special reserve
 - 20% of PGBP (before this deduction)
 - [200% of (share cap + general res.)] – opening bal in special reserve a/c
- NBFCs – not eligible

RECOGNITION OF INTEREST INCOME - I

s. 43D

- Overrides other provisions of the Act
 - s.28, 145, ICDS
- Applies to income by way of ‘interest’ of prescribed NBFC
- Relating to prescribed category
- Of Bad and Doubtful debts
- Rules 6EA and 6EB
- Having regard to RBI Guidelines
- NBFC being
 - deposit taking
 - non – deposit taking systemically important
 - clause (e), (f) & (g) of explanation to s.43B

RECOGNITION OF INTEREST INCOME - II

s. 43D

- Chargeability to tax
 - year of credit of interest
 - to Profit and Loss Account
- Applicability to be examined
 - year of actual receipt for NBFC
 - ‘accrued but not accounted’
 - impact of s.41
 - income from other sources – s.56
 - capital receipt
 - adjustment in cost of asset/construction
- IND AS permit deferment of interest to banks
 - but not to NBFC

INTEREST & GAINS ON BONDS

s. 4 & 5

- Recognition of interest for Subscriber
- Recognition of interest for Purchaser
- Recognition of gains/profits – on sale
- Recognition of gains/profits on redemption
- Treatment on purchase
- Claim for TDS
- Circular No. 599 dt. 24.04.1991
- Vijaya Bank Ltd 187 ITR 541 (SC)
- Circular No. 610 dt. 31.07.1991
- SLP in Citibank [Civil Appeal No. 1549 of 2006]
- Circular on DDB tax treatment
 - No. 2/2002, dt. 15.02.2002

INTEREST ON NPA

s. 4 & 5

- Interest on Loans, Advances & ICDs
- Debt has become NPA
- Non-receipt of interest
- S. 45Q of RBI Act
- Para 8(1) of ICDS IV
 - recognition of interest on passage of time at specified rate
 - Vasisth Chay Vyapar Ltd. 410 ITR 244 (SC)
 - Chamber of Tax Consultants 400 ITR 178 (Del.)
- Southern Technologies Ltd. 320 ITR 577 (SC)- significance

SIT v. INVESTMENT

s. 28 & 45

- Circular No. 599 dt. 24.04.1991
- Circular 665 dt. 05.10.1993
 - AO should determine on the facts and circumstances of each case taking into account the guidelines issued by the RBI
- Consequent treatment of losses relating to SIT

DEDUCTION OF INTEREST EXPENSE - I

s. 43B

- Overrides other provisions of Act
 - s.30 to 37 of the I.T. Act
- Applies to expenditure on interest
 - on loan or borrowing
 - from a prescribed NBFC
 - deposit taking
 - non – deposit taking systemically important
- Deductibility of such interest for any assessee
 - year of deduction on actual payment
 - in computing income u/s. 28

DEDUCTION OF INTEREST EXPENSE - II

s. 43B

- Year of incurring liability to pay – irrelevant
 - according to Method of Accounting
- Explanation 3AA – no deduction where allowed upto A.Y. 2019-20
- Explanation 3CA – no deduction for interest
 - converted into loan or borrowing
 - Issue of debenture, bond, etc, ‘not payment’
- Explanation 4(e) – deposit taking NBFC
 - 4(f) – Non – Banking Financial Company - s.45-I, clause (f)
 - 4(g) – Systemically important non deposit taking NBFC

DEDUCTION OF INTEREST EXPENSE - III

s. 43B

- Issues
 - interest on Advances
 - provisions of s.38 to s.40A , not applicable
 - interest where not in accordance with T&C of agreement
- Interest payable in kind
 - any sum payable
- Deduction against deemed income u/s.41(1)
- Explanation 3AA where deduction allowed for A.Y. 2020-21 onwards
 - actual payment in A.Y. 2021-22

M TO M LOSSES & ICDS VIII

s. 36(1)(xviii), 40A(13)

- M to M losses as per ICDS
 - allowed as deduction u/s. 36(1)(xviii)
- Notional losses not as per ICDS
 - Disallowed u/s. 40A(13)

EXPLANATION 1 AND PENALTY

s. 37(1)

- Prohibition on allowance of payment of fines & penalties
 - incurring expense is an offence or prohibited by law
- Applicable to NBFC as well

RATE OF TAX

s. 115BAA & 115BAB

- Provision for concessional rate of interest
 - s. 115BAA - 22% for companies
 - s. 115BAB - 15% for new manufacturing domestic companies
- NBFCs not eligible for s. 115BAB concession

MAT

s. 115JB

- S. 45-I of RBI
 - requires creation of reserves equivalent to 20% of profit
- Computation of book profit u/s. 115JB
- Profit as per Profit & Loss Account
- Adjustment as per Explanation to s. 115JB(2)
 - clause (b) & (c) for adjustment and add back
 - limited utilization of reserves
 - statutory reserves

TDS ON INTEREST ON FCB BY NBFC

s. 194LC

- Payment of interest by NBFC to non-resident
 - TDS @ 5%
 - TDS @ 4% for IFSC

TDS ON INTEREST ON BONDS BY NBFC

s. 194LD

- Interest on issue of bonds by NBFC to non-resident
 - TDS @ 5%

DISALLOWANCE OF EXPENDITURE

s. 14A

- Disallowance of 1% of AAMA
 - Rule 8D(2)(ii)
- Investment held as SIT
 - 14A not applicable
 - Nice Bombay Transport (P.) Ltd. 103 taxmann.com 338 (Delhi)
 - CCI LTD. 20 taxmann.com 196 (Kar.)
- Investment held as capital asset
 - 14A applicable
 - Tata Investment Corpn. Ltd. 113 TTJ 512(MUM.)

DEEMED DIVIDEND

s. 2(22)(e)

- Lending of money – substantial part of business
- Advance or loan
 - made in ordinary course of business
 - not regarded as deemed dividend
- Jayant H. Modi 28 taxmann.com 252 (Mum). ITAT

DISCRIMINATORY PROVISIONS

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SET OFF OF LOSSES

s. 72A

- Unabsorbed losses & depreciation
 - of amalgamating co.
 - deemed to be that of amalgamated or resulting company
- Permission to set-off
- Banking company eligible
- NBFCs not eligible

SPECULATION LOSSES

s. 73

- Explanation to s. 73
- Company engaged in the business of banking
 - losses shall not be deemed as speculative losses
- Not available to NBFCs

INTEREST ON EDUCATIONAL LOAN

s. 80E

- Applicable to individual & HUF
- Deduction of interest on educational loan taken from
 - financial institution
 - approved charitable institution
- NBFCs not eligible

THIN CAPITALISATION

s. 94B

- Interest expense in excess of Rs. 1 crore
 - by Indian co. or PE of foreign co.
 - to NR associate enterprise
- Limited to 30% of EBITDA
- Not applicable where
 - debt issued by a lender which is
 - PE of NR engaged in business of banking
- Applicable to NBFCs

TDS ON INTEREST

s. 194A

- TDS @ 10%
 - on interest other than "Interest on securities"
- Sub-section (1) not applicable
 - when income credited or paid in respect of
 - time deposits with
 - banking company
 - co-operative banks
 - deposits with public company in business of long term finance
- NBFCs - not eligible

TDS ON CASH WITHDRAWALS

s. 194N

- Cash withdrawals by any person from
 - banking co
 - co-operative soc. in business of banking
 - post office
- TDS @ 2% on cash withdrawals in excess of Rs. 1 crore
- Not applicable to any payment made to
 - government
 - banking or co-operative soc.
 - business correspondent of banks or co-operative banks
 - white label ATM operator
- NBFCs - not eligible

TDS ON SENIOR CITIZEN

s. 194P

- Banks to compute income of senior citizen & deduct TDS
 - after giving effect of
 - deduction under Chapter VI-A; and
 - rebate u/s. 87A
- Relief from filing ROI
- Senior citizen
 - resident in India;
 - 75 years or more;
 - pension & interest income
 - furnished declaration
- Not available to NBFCs

THANK YOU

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