Annexure 1 - Representation with respect to issues arising out of section 194R of the Act read with CBDT circular 12 of 2022

1. One time settlement of loans and loan waivers – case for exclusion *(concern arising out of Question no 3 of Circular 12 of 2022)*

Key concerns

1.1. NBFCs and other lending financial institutions (including Banks) are stringently regulated by the Reserve Bank of India (RBI).

1.2. One-time settlements reached with customers or, any waivers of loans granted on reaching settlements with the borrowers are done within the purview of the RBI regulatory framework[1] (including applicable master directions and circulars), and/or statutory process laid down under The Insolvency and Bankruptcy Code, 2016. Further, these settlements are subject to strict internal as well as external review processes (through Statutory Audit as well as RBI's periodical inspections and in case of IBC process, it is also subject to approval from the committee of creditors and the National Company Law Tribunal).

1.3. In the cases involving loan settlement/ waivers, the financial institution has already suffered significant loss of principal and interest in such cases. The schemes for waivers or one-time settlements are arrived at after all practically possible modes of recovery have been exhausted and no other choice is left with the financial institution but to bring matters to a close through a settlement. Most loan waivers would be in respect of accounts which have been classified as Non-Performing Assets (NPAs). There are RBI regulations which specify when a loan/Debtor has to be classified as NPA. Banks and Financial Institutions (FI) have stringent internal approval processes before such a waiver can be agreed to.

1.4. In case of one-time loan settlements and loan waivers, the entire proceedings are meant for the benefit of lenders, considering that in such cases, unless a negotiated settlement is entered, the prospects of recoverability of the amounts owed to the lenders would be bleak. Hence, while the outcome may possibly result in a benefit for borrower, from the lender's perspective, such schemes are not intended to grant any benefit or perquisite to the borrower. However, the Circular requires that for the purposes of applying section 194R of the Act, the financial institution should assume that a loan settlement or waiver as giving rise to a taxable benefit to the borrower – in fact this position is also contrary to the position established by many Courtsg, including that of the Supreme Court in *Commissioner v. Mahindra and Mahindra Ltd. [2018] 404 ITR 1 (SC)*.

1.5. While the circular allows the person responsible for deducting tax to seek tax payment/ recovery of taxes from the deductee, it is next to impossible to recover anything further from the

[1] RBI Regulatory framework comprises *inter-alia:*

a) For Banks, RBI Master Circular - "Prudential norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances" dated 1 April 2022 as updated from time to time
b) For NBFCs & HFCs, RBI Master Directions –
   - Master Direction - Non-Banking Financial Company - Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016 dated 1 September 2016 as updated from time to time
   - Master Direction - Non-Banking Financial Company – Non-Systemically Important Non-Deposit taking Company (Reserve Bank) Directions, 2016 dated 1 September 2016 as updated from time to time
   - Master Direction – Non-Banking Financial Company – Housing Finance Company (Reserve Bank) Directions, 2021 dated 17 February 2021 as updated from time to time

The aforesaid framework specifically covers various provisions relating to advances and where applicable, lending norms, restructuring, one time settlement, etc.

borrower, that is already struggling with the repayment of the loan. As such, it would become the financial institution's obligation to bear the taxes out of its own pocket (that too after grossing up), thus putting the financial institution's capital through further unwarranted strain.

1.6. Ironically, credit for such TDS would reflect in the Form 26AS of the borrower. In fact, it is quite likely that the borrower may have significant losses such that possibly even if the waiver benefit were to be taxed, there may possibly be no net tax liability in his hands. In such case, the borrower would in fact go on to claim refund of the TDS borne by the lender. In such situations, there is no benefit to the Revenue that has to ultimately refund the TDS with interest.

1.7. An example to this effect is outlined in '***Appendix-A'***, for your quick reference.

1.8. In other words, there is no control over the borrower claiming credit for such TDS which would amount to unjust enrichment for the borrower as the Banks and FI have borne the tax liability.

1.9. It may also be noted that such an outcome can also never be the intention of a one-time loan settlement or waiver agreement as it defeats the very object of such settlement. Effectively the financial institution may be seen as extending an additional benefit to the defaulting borrower, which may not be taken very kindly by the RBI or other regulators.

1.10. In any event, if the idea is only to track the relevant borrowers deriving a benefit with a view to levy tax in the borrower's hands, the same may be tracked through disclosures already being made by financial institutions as part of their tax filing in ITR-6 tax return form. The disclosure (currently, PAN of borrowers is required to be disclosed on account of bad debts written off in excess of INR 1 lakh) may need fine-tuning to specifically reflect one time settlement or waiver cases.

1.11. *Relief Sought*

1.11.1. We thank the CBDT for understanding and appreciating the difficulties explained above by the FIs (banks and NBFCs) from the purview of section 194R in the context of one-time settlements of loans and loan waiver agreements reached by such institutions with borrowers.

1.11.2. We also understand that it may not be possible to exclude all such FIs.

Therefore, we have proposed for your kind consideration, the possible list of financial institutions, which may be excluded from the applicability of section 194R in respect of any one-time settlement or loans waiver agreements:

***"Lenders eligible for benefit under section 43D of the Income-tax Act*:**

a) Public Financial Institution (being a company under section 4A of the Companies Act, 1956)
b) Scheduled Bank;
c) Co-operative Bank other than a primary agricultural credit society (governed by the Banking Regulation Act, 1949);
d) Primary Co-operative Agricultural and Rural Development Bank (governed by NABARD as mentioned in the Banking Regulation Act, 1949);

e) State Financial Corporation (governed by the State Financial Corporations Act, 1951);

f) State Industrial Investment Corporation (means a Government company within the meaning of section 617 of the Companies Act, 1956)

g) Deposit taking Non-Banking Financial Company ('NBFC-D');

***h)* Systemically Important Non-Deposit Taking NBFC (SI-ND-NBFC);**

i) Public company engaged in providing long term finance for construction or purchase of houses in India for residential purposes and which is registered in accordance with the guidelines/ directions issued by the National Housing Bank – formed under National Housing Bank Act, 1987[2];

Additionally, it is prayed that exclusion should also be provided to:

j) Asset Reconstruction Companies ('ARCs') registered under Section 3 of the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest (SRFAESI) Act, 2002.

(Please note that an ARC is regulated by RBI as a NBFC under section 45(f)(iii) of the RBI Act, 1934)

[2] HFCs is treated as one of the categories of Non-Banking Financial Companies (NBFCs) for regulatory purposes and RBI carries out a review of the extant regulatory framework applicable to the HFCs.

2. Clarification for certain expenses in relation to events (concern arising out of Question No. 4 of CBDT Circular 12 of 2022)

2.1. When businesses host events, there is always a primary business purpose and this is also recognized in Question No. 8 of circular 12 of 2022. Hosting events have always been an established way for businesses to not just meet and accomplish various business objectives, but also develop deeper business relationships.

2.2. *Expenditure pertaining to the day immediately prior to and the day immediately after the conference dates ought not to be regarded as giving rise to any benefit and perquisite*

2.2.1 Whilst the clarification that all expenses pertaining to dealer/ business conference (which shall generally include travel, food and accommodation) during the conference dates would not be considered as benefit and perquisite is welcome.

However, you would appreciate that the events are usually held at a venue which is central and easier for people from different locations to travel to. Out of necessity and other logistical challenges like flight availability, some participants may need to come a day earlier or leave a day later.

2.2.2 To avoid any future disputes, it may also be clarified that all the expenses (other than leisure) on participants of dealer/ business conference pertaining to a day immediately prior to and the day immediately after the conference dates ought not to be regarded as overstay giving rise to any benefit and perquisite.

2.3. *Option to forego the expenses on leisure as a deduction vs compliance with section 194R*

From the perspective of leisure component, where TDS under section 194R is envisaged, to ease the administrative hassle envisaged in levying tax under section 194R, an alternative could be considered whereby the assessee could be given an option to forego the claim for deduction of the expenses on the "leisure element" of events as an alternative to compliance with section 194R of the Act, subject to consequential relaxations being allowed from interest and penalties.

2.4. ***Relief sought***

1. It may be clarified that all expenses (other than pertaining to leisure) for the day immediately prior to and the day immediately after the conference dates should not be regarded as "overstay" giving rise to any benefit and perquisite so as to attract section 194R.

2. Given the hardship involved in implementation of the changes with immediate effect, taxpayers should be provided an option to forego the claim for deduction of the expenses on the "leisure element" of events as an alternative to complying with section 194R of the Act, subject to consequential relaxations being allowed from interest and penalties.

3. Payments already subject to TDS under other sections of Chapter XVII-B or pure reimbursements
(concern arising out of Question No. 7 of CBDT Circular 12 of 2022)

3.1. Currently, taxes are deductible from amounts payables by way of fees for professional or technical services under section 194J or for payment to contractors under section 194C or payment of commission under section 194H or payment of insurance commission under 194D, etc.

3.2. To explain the issue with an example involving payment of fees under section 194C of the Act, the service provider may incur certain expenses wholly and exclusively for provision of services like travelling, accommodation, etc. These are generally reimbursed by the services recipient pursuant to the contractual agreement. Question No. 30 of CBDT Circular No. 715 dated 8 August 1995 has clarified that reimbursement amount raised in invoice should be included for TDS under section 194C and 194J of the Act. Accordingly, these reimbursements are already subject to TDS at rates applicable under these sections.

3.3. CBDT Circular 12 of 2022 stipulates that reimbursement of expenses by the client wherein invoices are in the name of the client (and not the professional or contractor) should not be subject to TDS under section 194R of the Act. As a corollary, where the invoices are in the name of the professional / contractor and reimbursement is sought, section 194R may be attracted.

3.4. This position is contrary to the position set out in CBDT Circular No. 715 as well as CBDT Circular No. 720 dated 30-8-1995 which seeks to avoid duplication in the levy of TDS. This would cause uncertainty and dispute around which section is applicable.

3.5. *GST in the name of the consultant or service provider*

The fact that in a given case (although this may not happen in all cases) credit for GST on a charge (say legal expenses) may be taken by the business associate/ consultant and then reimbursement is claimed, that by itself should not give rise to a presumption that the liability to bear/ reimburse the charge belongs to that party such that there arises a need to withhold taxes under section 194R.
The right of the party to recover out of pocket expenses or any costs incurred in the course of providing services should be seen as independent of any accounting entries or GST input credit availment.

In this respect, especially where the reimbursement is already subject to tax under some other section, the mere fact that GST credit has been availed by such vendor or service provider ought not to attract the levy of TDS under section 194R of the Act.

3.6. ***Relief sought :***

With a view to clear the doubts and avoid the hardships, a clarification should be issued to provide for exclusion from the TDS provisions under section 194R for payments which are already subject to TDS under any other section of Chapter XVII-B of the Act.

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4. Invoices in the names of vendors or service providers or cases of pure reimbursements ***(concerns arising out of Question No. 7 of CBDT Circular 12 of 2022)***

4.1. Question No. 7 of CBDT Circular 12 of 2022 has clarified that reimbursement of expenses by the client wherein invoices are in the name of the client (and not the service provider) should not be subject to TDS under section 194R of the Act.

4.2. As a possible corollary, where the invoices are in the name of the professional / contractor and reimbursement is sought, section 194R may be considered as attracted.

4.3. Companies during the course of their business have to bear or reimburse certain expenses where the invoices may be in the name of a third party.

4.4. Examples of such cases could include statutory dues (such as stamp duties), electricity bill, premises maintenance charges etc. where bill may be in the name of the service provider including landlord, etc.

4.5. The fact that companies have to either reimburse or bear the costs of these charges ought not to give rise to a presumption that there is a benefit / perquisite in the hands of recipient so as to attract TDS under section 194R.

4.6. Further, to the extent, an item is a pure reimbursement of a statutory levy (e.g. stamp duty) or an expense borne on account of contractual obligation of the business (e.g. electricity or society maintenance), there ought to be no levy of any TDS including under section 194R in the hands of the service provider/ landlord as the case may be.

4.7. ***Relief sought***

A clarification may be issued that statutory dues and other items being borne by or reimbursed by the business should not be regarded as benefit / perquisite in the hands of service provider/ recipient so as to attract section 194R of the Act.

An indicative list of such items are as below:

- ***Taxes deducted at source under section 194R***
- ***Stamp duty***
- ***Electricity bill in landlord's name***
- ***Repairs & maintenance charges paid to housing society***

Appendix-A

Illustration: Typical situation where borrower is in a loss situation and would not be required to offer the loan waiver (classified as benefit) as income and hence claims the tax paid under section 194R as refund

Sr. No.	Particulars	Existing scenario	After section 194R	Diff in Tax
	In the books of lender			
1	Outstanding loan of ABC Ltd.	1,000,000	1,000,000	
2	Amount recovered by Lender under OTS scheme	(730,000)	(730,000)	
3	**Waiver of loan by** Lender **under OTS scheme** *(1-2)*	**270,000**	**270,000**	
4	TDS under section 194R @10% (borne by lender & hence, grossed up)	-	30,000	30,000
5	**Total Loss to** lender **as waiver of loan (claimed under section 36(1)(vii)** *(3-4)*	**270,000**	**300,000**	
6	Tax impact of deduction claimed by lender (@25% approx.) *(25% of 5)*	(67,500)	(75,000)	(7,500)
7	**Net Loss to** lender *(6-7)*	**202,500**	**225,000**	
	In the Books of ABC Ltd			
1	Benefit / Perquisite under OTS to ABC	270,000	300,000	
2	Accumulated losses (assumed)	350,000)	(350,000)	
3	**Net taxable income** *(1-2)*	**(80,000)**	**(50,000)**	
4	Tax payable on net taxable income (@25% approx.) *(25% of 3) (NIL if negative)*	-	-	
	TDS credit claimed by ABC Ltd	-	30,000	
6	**Likely refund to ABC Ltd** *(4-5)*	**-**	**(30,000)**	30,000)
	Net tax revenue / (loss) to government			**(7,500)**