

Issues in GST on Banking Sector

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Introduction:

Banking sector plays a very crucial role in a macro economic and monetary policies of any country overall framework and the business dynamics of this sector largely differs from other sectors. The regulatory framework for this sector is very strong and leaves no room for any discrepancies. Unlike, other businesses where there are many un-organised ways of style of workings still prevail, same is not the case with this sector which is largely organised in nature. Therefore, any issues for this sector has to be closely looked at and timely resolved so to that larger economic interest of the nation is achieved. This article lay down various issues that a Banking sector may face due to advent of GST and the suggestions so as to amend the rules, wherever required to be address the negative impact of GST on the Banking sector. Various aspects discussed herewith would apply to all types of banks viz., Nationalised Banks, Private Banks, Public Banks, Co-operative Banks etc. However, the article does not lay discussion on Non-Banking Financial Companies (NBFC's), Micro Finance companies, Credit Cooperative societies etc.

1) State-wise Registration requirement:

Currently, all banks have a centralized registrations under the Service Tax laws for all its branches. Banks having branches in multiple states & Union Territories (UT) will be required to obtain registrations in each such state & Union Territory in the GST regime. Such a requirement will have huge compliance burden on the banks. Further, high coordination and control between the banks within and outside state for tax matters needs to be placed. Moreover, under GST, accounting, administration, financial records etc, would be required to be maintained for each state-wise separately. This will be highly cumbersome and challenging. Since, it will be difficult for the Banks to cope up with such radical change of taking state-wise registrations, filing multiple returns state-wise, multiple audits and assessments; especially in a scenario where banks have presence in almost every state and union territory of the country and with each state, each city, each locality has a branch of the bank.

Further, even state-wise regional banks do not have capabilities to coordinate and receive information from all the branches within the state and comply with the tax requirements. With so many braches, the

entire coordination and assimilation of information at one place for compliance by each state regional bank shall also be a challenge. Therefore, government must provide for some special scheme to the banking sector so that the high administration and compliance burden as placed under the GST is reduced as the business dynamics of banking sector largely differs from that of other industries.

2) Inter-state supplies of goods or services (or both) between two branches of the same bank:

Presently, transactions between branches were not subjected to any taxes. However, this is taxable in the GST regime. Inter-state supplies of goods or services (or both) between two branches of the same bank, located in two States, will attract IGST. Generally, banks would have lot of common/ shared services being supported from Head Office such as call centre, security software etc. Further, many times one branch would internally provide service to other branches for example: resolving issue of a customer having PAN India accounts, providing local information etc. to other branches etc. If GST is to be charged on such supplies, even though the same are made without consideration, it would cause unnecessary hardship. Although, relief is provided in the valuation rules that in case of a transaction with distinct persons, value disclosed on the invoice shall be deemed to be taken as an open market value, however still valuation issues may creep as this rule does not apply if the receiving branch is not able to avail the full credit due to any reason whatsoever. Since, in a banking sector tracking such transactions would prove to be a cumbersome task and lead to multiple interpretations and disputes, therefore we suggest that by virtue of Rule 6(7) of GST Valuation Rules, banking services be categorised in such class of services where value for any transactions undertaken between the distinct persons is deemed to be considered as Nil.

3) Place of supply in case of banking services:

Under GST Law the place of supply of services for banking and other financial services (BOFS) shall be the location of the recipient of services on the records of the supplier of services. Provided that if the location of recipient of services is not on the records of the supplier, the place of supply shall be the location of the supplier of services.

However, what constitutes the 'records of the supplier' is not defined in the law leading to multiple interpretations as to whether it is to be understood as accounting records or customer records, vendor records and so on. Further, in some cases banks would have multiple addresses of the same customer in its records, this is possible as in case of a banking sector a customer would add multiple accounts within the same customer id and in which case only one address of the customer under whose address that customer id is registered would be reflected as the address on records.

However it is possible that the transaction is undertaken with the account holder within the same customer id but having a branch in different state. In such a situation, if strictly banks pay GST to the state based on the "address on record" then it may end up paying GST in a wrong state. Therefore, banks have to record the address of each account holders within the same customer id and GST needs

to be charged on that account holder and accordingly tax also must be paid to that respective state government of the account holder and not the single address captured for the entire customer id. E.g. it is quite possible that bank issues 'bank guarantee' to be submitted to a local authority by a company. Now, if as per the bank's records, address of the customer [as its HO] is mentioned/ maintained where such address is in the other state, wrong GST may get levied.

It is in this background, it is suggested to bring suitable clarity in the place of supply provisions in this regard and the term "Address on Records" be clearly defined to avoid any disputes as to determination of place of supply.

4) Reversal of Input Tax Credit on Capital Goods:

Presently, as per Rule 6(3B) of CENVAT Credit Rules, 2004, an assessee in banking sector has to reverse 50% of the CENVAT Credit taken on monthly basis on inputs and input services. However, banks can take full credit on Capital goods unless the said capital goods are exclusively used for any exempted service.

However, section 17(4) of the GST law states that banks engaged in supplying services by way of accepting deposits, extending loans or advances have to reverse 50% of the eligible input tax credit on inputs, *capital goods* and input services.

It is pertinent to note that requirement of reversal of standard 50% credit even on the capital goods portion will have negative impact. Various office furniture, equipments, cash-counting machines, computers, printers, air-conditioners etc. are of high procurement cost for any branch of the bank and if 50% of the credit on the same is to be reversed then it shall have an adverse impact.

Further, since all the capital assets are used for common services, therefore. ITC of only 50% in respect of the capital goods gets allowed. Therefore, we suggest that the provision of reversal of 50% credit for capital goods must be removed. Alternatively, the same may be brought in line with the current service tax law and the credit for capital goods must be available in maximum of 2 years as per the present service tax law.

5) Reversal of Input Tax credit over and above standard 50%:

As per the provisions of the GST Act, option has been given to bankers to reverse 50% of the CENVAT credit instead of reversing based on the input service partly attributable to the taxable supply and exempted supplies. Similar provision is also in place under Service Tax law. However, it is noted that departmental notices are being issued demanding to reverse CENVAT credit of input, input services that are exclusively used for exempted services even though the option for reversal of credit at 50% is opted for.

It is therefore suggested to have a specific clause incorporated stating that once the option to reverse tax at 50% is opted, then there should not be any conditions imposed over actual correlation of output services/ goods with input services/ goods for the purpose of rejection of credits.

In such scenario, the entire tax paid for the procurement of goods and services, irrespective of whether the same are directly or indirectly used for the taxable or exempted supplies can be easily reversed at a specified reversal percentage without any distortions as to interpretation of the law.

6) Taxability of Interest:

Presently, interest income and discount provided by the banks are covered under negative list, hence not taxable to service tax. Under GST, the term 'service' is defined in a wide manner to cover 'anything other than goods' which may cover interest as well. Governments across the world do not levy GST on interest. The GST Law in India too should clarify if interest is outside the ambit of GST. If 'interest' is not expected to attract GST, it will have implications on input tax credits claimed by banks. Further, such a move would have larger economic issues. Therefore, we suggest to follow the current scenario where in the service tax law, interest is kept in the negative list, similarly interest can be kept in schedule 3 of the GST law so that it neither amounts to supply of good nor service and therefore no GST would be applicable on the same.

7) Sale of Repossessed Assets:

When a bank re-possesses assets from a defaulter of loan & sales them, VAT is paid by the bank as a 'dealer' under state VAT laws in some States. The litigation continues as to whether, the bank effects the sale of such assets or facilitates/ compels the sale of assets by the defaulting borrower or as the case may be, Bank has acted as an agent of the defaulting borrower to sale/dispose off the asset. Such sales are effected to realise the bad/sticky loans of such banks. In GST Law, if Banks are treated as suppliers of such assets, the overall cost of operations for Banks would go up, as it is expected that the rate of GST would be higher than the present VAT rate. Therefore, it is expected that the rate of such transactions should not be pegged under the category of standard rate @ 18% and instead the same should be at a lower rate of 5%. Further, banks would take possession and control over under-constructed buildings if there is lapse in payment of instalments, in such a scenario building would be sold before the receipt of completion certificate or first occupancy. A suitable clarity has to be provided whether in this situation GST would be applicable or whether it will not be treated as supply by virtue of clause 5 of schedule 3 and not be taxable under GST since it is sale of immovable property.

8) Value for reversal of Input Tax Credit:

Presently, as per Rule 6(3B) of CENVAT Credit Rules, 2004, an assessee in banking sector has to reverse 50% of the CENVAT Credit taken on monthly basis or follow the procedure for reversal as per Rule 6(3) i.e. reversal on actual basis. However, if reversal is made on actual basis, then it is specifically provided that 'Value' for the purpose of calculation of reversal shall not include the value of service by way of "extending deposits, loans or advances" against consideration in the form of 'interest' or 'discount'.

