

# CIRCULAR ON APPLICABILITY OF GST ON ADDITIONAL OR PENAL INTEREST



In the present article we are going to discuss and after discussion have a clarification on **Applicability of GST on Additional or Penal Interest** in case of late payment of Equated monthly installment.

Department has received so many representations from the trade and industry regarding the applicability of GST on delayed payment charge in case of late payment of Equated Monthly Installment(EMI).

Before moving ahead its good to have a little idea about **EMI**.

The concept of EMI is explained in the next page.

Equated Monthly Installment  
EMI

An EMI is a fixed amount paid by a borrower to a lender at a specified date every calendar month.

EMIs are used to pay off both interest and principal every month, so that over a specified period, the loan is fully paid off along with interest

In cases where the EMI is not paid at the scheduled time, there is a levy of additional / penal interest on account of delay in payment of EMI.

Doubts were there on whether additional/ penal interest on the overdue loan would be exempt from GST in terms of Sl. No. 27 of notification No. 12/2017-Central Tax (Rate) dated 28th June 2017 or such penal interest would be treated as consideration for liquidated damages [amounting to a separate taxable supply of services under GST covered under entry 5(e) of Schedule II of the Central Goods and Services Tax Act, 2017 (hereinafter referred to as the CGST Act) i.e. “agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act”].

## clarification

In order to provide uniformity in the provision of the law, Board has issued following clarification- Board says that, Generally the following two transaction options involving EMI are prevalent in trade.

**Case no.1-** X sells a mobile phone to Y. The cost of mobile phone is Rs 40,000/-. However, X gives Y an option to pay in installments, Rs 11,000/- every month before 10th day of the following month, over next four months. Further, as per the contract, if there is any delay in payment by Y beyond the scheduled date, Y would be liable to pay additional / penal interest amounting to Rs. 500/- per month for the delay. In some instances, X is charging Y Rs. 40,000/- for the mobile and is separately issuing another invoice for providing the services of extending loans to Y, the consideration for which is the interest of 2.5% per month and an additional / penal interest amounting to Rs. 500/- per month for each delay in payment.

**Case No.2-** X sells a mobile phone to Y. The cost of mobile phone is Rs 40,000/-.Y has the option to avail a loan at interest of 2.5% per month for purchasing the mobile from M/s ABC Ltd. The terms of the loan from M/s ABC Ltd. allows Y a period of four months to repay the loan and an additional / penal interest @ 1.25% per month for any delay in payment.

The provision of sub clause (d) of sub-section (2) of section 15 of the CGST Act says that the value of Supply shall include “interest or late fee or penalty for delayed payment of any consideration for any supply”. Further in terms of Sl. No. 27 of notification No. 12/2017- Central Tax (Rate) dated the 28.06.2017 “services by way of (a) extending deposits , loans or advances in so far as the consideration is represented by way of interest or discount( other than interest involved in credit card services)” is exempted.

Further, as per clause 2 (zk) of the notification No. 12/2017-Central Tax (Rate) dated the 28th June, 2017, “‘interest’ means interest payable in any manner in respect of any moneys borrowed or debt incurred (including a deposit, claim or other similar right or obligation) but does not include any service fee or other charge in respect of the moneys borrowed or debt incurred or in respect of any credit facility which has not been utilised;”.



The conclusion has been given as per case 1. and case 2. as given above.

Case 1.- As per the provisions of sub-clause (d) of sub-section (2) of section 15 of the CGST Act, The amount of penal interest is to be included in the value of supply. Transaction between X and Y is for supply of taxable goods i.e. mobile phone. Accordingly, the penal interest would be taxable as it would be included in the value of the mobile, irrespective of the manner of invoicing.

Case 2.- The additional / penal interest is charged for a transaction between Y and M/s ABC Ltd., and the same is getting covered under Sl. No. 27 of notification No. 12/2017- Central Tax (Rate) Accordingly, the 'penal interest' charged thereon on a transaction between Y and M/s ABC Ltd. would not be subject to GST. The value of supply of mobile by X to Y would be Rs. 40,000/- for the purpose of levy of GST.



It is clarified that the transaction of levy of additional / penal interest does not fall within the ambit of entry 5(e) of Schedule II of the CGST Act, As this levy of additional / penal interest satisfies the definition of “interest” as contained in notification No. 12/2017- Central Tax (Rated). It is further clarified that any service fee/charge or any other charges that are levied by M/s ABC Ltd. in respect of the transaction related to extending deposits, loans or advances does not qualify to be interest as defined in notification No. 12/2017- Central Tax (Rate), and accordingly will not be exempt.