



2024:KER:58193

IN THE HIGH COURT OF KERALA AT ERNAKULAM

PRESENT

THE HONOURABLE MR. JUSTICE GOPINATH P.

MONDAY, THE 29<sup>TH</sup> DAY OF JULY 2024 / 7TH SRAVANA, 1946

WP(C) NO. 24617 OF 2022

PETITIONER:

MANAPPURAM FINANCE LTD,  
MANAPPURAM HOUSE, VALAPAD PO, THRISSUR, PIN - 680 567,  
REPRESENTED BY GENERAL MANAGER  
M/S MANAPPURAM FINANCE LTD., SHRI M.V. BABU,  
S/O. M.T. VARGHESE, AGED 73 YEARS,  
RESIDING AT MAZHUVANCHERRY PARAMBATH HOUSE, AYYAMPILLY,  
ERNAKULAM, PIN - 682 501.

BY ADVS.

V. RAGHURAMAN (SR.)  
BHANUMURTHY  
K.S.BHARATHAN  
AADITHYAN S.MANNALI  
ALPHIN ANTONY  
VISAKH ANTONY  
CHRISTINE MATHEW  
RANCE R.

RESPONDENTS:

- 1 THE UNION OF INDIA,  
MINISTRY OF FINANCE, REPRESENTED BY SECRETARY,  
NORTH BLOCK, NEW DELHI, PIN - 110 001.
- 2 THE CENTRAL BOARD OF EXCISE AND CUSTOMS,  
REPRESENTED BY CHAIRMAN, ROOM NO. 227-B,  
DEPARTMENT OF REVENUE, NORTH BLOCK, NEW DELHI,  
PIN - 110 001.
- 3 THE ADDITIONAL DIRECTOR GENERAL,  
GOODS AND SERVICES TAX INTELLIGENCE, KOCHI ZONAL UNIT,  
CENTRAL EXCISE BHAWAN, KATHRIKADAVU, KALOOR P.O, KOCHI,  
PIN - 628 017.



- 4 THE ADDITIONAL /JOINT COMMISSIONER OF CENTRAL TAX,  
KOCHI CENTRAL TAX COMMISSIONERATE,  
CENTRAL REVENUE BUILDING, I.S PRESS ROAD, KOCHI,  
PIN - 682 108.
  
- 5 THE STATE OF KERALA,  
REPRESENTED BY ITS SECRETARY, TAXES DEPARTMENT,  
GOVERNMENT SECRETARIAT, THIRUVANANTHAPURAM,  
PIN - 695 001.

BY ADVS

SREELAL N. WARRIER (SC)  
JASMINE M.M (GP)

THIS WRIT PETITION (CIVIL) HAVING BEEN FINALLY HEARD ON  
29.07.2024, THE COURT ON THE SAME DAY DELIVERED THE FOLLOWING:



## **JUDGMENT**

The issues raised in this writ petition appear to be covered in favour of the petitioner in the light of clarifications issued vide Circular No.204/16/2023-GST dated 27-10-2023 and also by Circular No.218/12/2024-GST dated 26-06-2024 issued by the GST Policy Wing, Central Board of Indirect Taxes and Customs, Department of Revenue, Ministry of Finance, Government of India. The questions raised are whether any GST is payable on reverse charge basis on supply of services by the Managing Director of the company by way of providing personal guarantee on loans taken by the company and whether any GST is payable on supply of services by way of extending loans by the petitioner-company to its subsidiary company. In Circular No.204/16/2023-GST dated 27-10-2023 it was clarified as follows:

<b>Sl. No.</b>	<b>Issue</b>	<b>Clarification</b>
1	Whether the activity of providing personal guarantee by the Director of a company	As per Explanation (a) to section 15 of CGST Act, the director and the company are to be treated as related persons. As per clause (c) of sub-section (1) of



<p>to the bank/ financial institutions for sanctioning of credit facilities to the said company without any consideration will be treated as a supply of service or not and whether the same will attract GST or not.</p>	<p>section 7 of the CGST Act, 2017, read with S. No. 2 of Schedule I of CGST Act, supply of goods or services or both between related persons, when made in the course or furtherance of business, shall be treated as supply even if made without consideration. Accordingly, the activity of providing personal guarantee by the Director to the banks/ financial institutions for securing credit facilities for their companies is to be treated as a supply of service, even when made without consideration.</p> <p>Rule 28 of Central Goods and Services Tax Rules, 2017 (hereinafter referred to as "CGST Rules" ) prescribes the method for determining the value of the supply of goods or services or both between related parties, other than where the supply is made through an agent. In terms of Rule 28 of CGST Rules, the taxable value of such supply of service shall be the open market value of such supply.</p> <p>RBI has provided guidelines for obtaining personal guarantee of promoters, directors and other managerial personnel of the borrowing concerns vide Para 2.2.9 of its <u>Circular No. RBI/2021-22/121</u> dated 9<sup>th</sup> November, 2021, which is reproduced below:</p> <p><b><i>"2.2.9 Guidelines relating to obtaining of personal guarantees of promoters, directors, other managerial personnel, and shareholders of borrowing concerns</i></b></p> <p><i>Banks should take personal guarantees of promoters, directors, other managerial personnel or major shareholders for the credit facilities granted to corporates, public or private, only when absolutely warranted after a careful examination of the circumstances of the case and not as a matter of course. In order to identify the circumstances under which the guarantee may or may not be considered necessary, banks should be guided by the</i></p>
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		<p><i>following broad considerations:</i>  .....</p> <p><b><i>C. Worth of the guarantors, payment of guarantee commission, etc</i></b></p> <p><i>Where personal guarantees of directors are warranted., they should bear reasonable proportion to the estimated worth of the person. <b>The system of obtaining guarantees should not be used by the directors and other managerial personnel as a source of income from the company. Banks should obtain an undertaking from the borrowing company as well as the guarantors that no consideration whether by way of commission, brokerage fees or any other form, would be paid by the former or received by the latter, directly or indirectly. This requirement should be incorporated in the bank's terms and conditions for sanctioning of credit limits. During the periodic inspections, the bank's inspectors should verify that this stipulation has been complied with. There may, however, be exceptional cases where payment of remuneration may be permitted e.g. where assisted concerns are not doing well and the existing guarantors are no longer connected with the management but continuance of their guarantees is considered essential because the new management's guarantee is either not available or is found inadequate.</b></i>  ..... "</p> <p>Accordingly, as per mandate provided by RBI in terms of Para 2.2.9 (C) of RBI's <u>Circular No. RBI/2021-22/121</u> dated 9<sup>th</sup> November, 2021, no consideration by way of commission, brokerage fees or any other form, can be paid to the director by the company, directly or indirectly, in lieu of providing personal guarantee to the bank for borrowing credit limits. As such, when no consideration can be paid for the said transaction by the company to the</p>
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		<p>director in any form, directly or indirectly, as per RBI mandate, there is no question of such supply/ transaction having any open market value. <b>Accordingly, the open market value of the said transaction/ supply may be treated as zero and therefore, taxable value of such supply may be treated as zero. In such a scenario, no tax is payable on such supply of service by the director to the company.</b></p> <p>There may, however, be cases where the director, who had provided the guarantee, is no longer connected with the management but continuance of his guarantee is considered essential because the new management's guarantee is either not available or is found inadequate, or there may be other exceptional cases where the promoters, existing directors, other managerial personnel, and shareholders of borrowing concerns are paid remuneration/ consideration in any manner, directly or indirectly. In all these cases, the taxable value of such supply of service shall be the remuneration/ consideration provided to such a person/ guarantor by the company, directly or indirectly.</p>
	xxx	xxx

The above Circular takes care of the first issue raised in this writ petition. The second issue is covered by the clarification given in Circular No.218/12/2024-GST dated 26-06-2024 where it was clarified as follows:



Sl. No.	Issue	Clarification
<b>Clarification regarding taxability of the transaction of providing loan by an overseas entity to its Indian related entity or by a person in India to a related person</b>		
1	Whether the activity of providing loans by an overseas affiliate to its Indian affiliate or by a person to a related person, where there is no consideration in the nature of processing fee/ administrative charges/ loan granting charges etc., and the consideration is represented only by way of interest or discount, will be treated as a taxable supply of service under GST or not.	<p>1. As per clause (c) of sub-section (1) of section 7 of the CGST Act, read with S. No. 2 and S. No. 4 of Schedule I of CGST Act, supply of goods or services or both between related persons, when made in the course or furtherance of business, shall be treated as supply, even if made without consideration. Therefore, it is evident that the service of granting loan/ credit/ advances by an entity to its related entity is a supply under GST.</p> <p>2. Services by way of extending deposits, loans or advances <b>in so far as the consideration is represented by way of interest or discount</b> (other than interest involved in credit card services) are exempted under sub entry (a) of entry 27 of <u>Notification No. 12/2017-Central Tax (Rate)</u>. Therefore, it is clear that the supply of services of granting loans/ credit/ advances, in so far as the consideration is represented by way of interest or discount, is fully exempt under GST.</p> <p>3. It is mentioned that overseas affiliates or domestic related persons are generally charging no consideration in the form of processing fee/ service fee, other than the consideration by way of interest or discount on the loan amount. Doubts are being raised regarding the taxability of the services of processing/ administering/ facilitating the loan in such cases, by deeming the same as supply as per clause (c) of sub-section (1) of section 7 of the CGST Act, read with S. No. 2 and S. No. 4 of Schedule I of CGST Act. The <b>processing fee/ service fee</b> is generally a one-time charge that lenders levy on applicants when they apply for a loan. This fee is generally non-refundable and</p>



		<p>is used to cover the <b>administrative cost of processing the loan application</b>. Charges of any other nature in respect of loan, other than by way of interest or discount, would represent taxable consideration for providing the facilitation/ processing/ administration services for the loan and hence would be liable to GST. This has been clarified at serial number 42 in the <u>Sectoral FAQ on Banking, Insurance and Stock Brokers Sector</u> issued by CBIC.</p> <p>4. It is significant to note that the processing/ service fee is generally charged by the bank/ financial institution from the recipient of the loan in order to cover the administrative cost of processing the loan application. An independent lender may carry out a thorough credit assessment of the potential borrower to identify and evaluate the risks involved and to consider methods of monitoring and managing these risks. Such credit assessment may include understanding the business of the applicant, as well as the purpose of the loan, financial standing and credibility of the applicant, how it is to be structured and the source of its repayment which may include analysis of the borrower's cash flow forecasts, the strength of the borrower's balance sheet, and where any collateral is offered, due diligence on the collateral offered may also be required to be carried out. To cover such costs, the independent lender generally collects a fee that is in the nature of processing fee/ administrative charges/ service fee/ loan granting charges, which is leviable to GST.</p> <p>5. However, when an entity is extending a loan to a related entity, it may not require to follow such processes as are followed by an independent lender. For example, it may not need to go through the same process of information gathering about the borrower's business, his financial standing and credibility and other details, as the required information may already</p>
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	<p>be readily available within the group, or between related persons. The lender may not also take any collateral from the borrower. Accordingly, in case of loans provided between related parties, there may not be the activity of 'processing' the loan, and no administrative cost may be involved in granting such a loan. Therefore, it may not be desirable to place the services being provided for processing the loans by banks or independent lenders vis-a-vis the loans provided by a related party, on equal footing.</p> <p>6. Even in case of loans provided between unrelated parties, there may not be any processing fee/ administrative charges/ loan granting charges etc., based on the relationship between the bank/ independent lender and the person taking the loan. The lender might waive off the administrative charges in full, based on the nature and amount of loan granted, as well as based on the relationship between the lender and the concerned person taking the loan.</p> <p>7. Accordingly, in the cases, where no consideration is charged by the person from the related person, or by an overseas affiliate from its Indian party, for extending loan or credit, other than by way of interest or discount, it cannot be said that any supply of service is being provided between the said related persons in the form of processing/ facilitating/ administering the loan, by deeming the same as supply of services as per clause (c) of sub-section (1) of section 7 of the CGST Act, read with S. No. 2 and S. No. 4 of Schedule I of CGST Act. Accordingly, there is no question of levy of GST on the same by resorting to open market value for valuation of the same as per rule 28 of Central Goods and Services Tax Rules, 2017.</p> <p>8. However, in cases of loans provided between related parties, wherever any fee</p>
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		in the nature of processing fee/ administrative charges/ service fee/ loan granting charges etc. is charged, over and above the amount charged by way of interest or discount, the same may be considered to be the consideration for the supply of services of processing/ facilitating/ administering of the loan, which will be liable to GST as supply of services by the lender to the related person availing the loan.
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The Circulars issued by the Central Board are binding on the authorities.

2. The learned Senior Standing Counsel appearing for the respondent department does not dispute that the issues raised are covered by virtue of the clarifications given in the Circulars referred to above. It is not disputed that the impugned show cause notice does not deal with any other issue.

In the light of the above and without going into the merits of any other contention taken in the writ petition, this writ petition is allowed and Ext.P1 show cause notice will stand quashed.

**Sd/-**

**GOPINATH P.  
JUDGE**

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**APPENDIX OF WP(C) 24617/2022****PETITIONER'S EXHIBITS**

- Exhibit P1** TRUE COPY OF THE SHOW CAUSE NOTICE DATED 20.04.2022 BEARING NO. 07/2022-23 ISSUED BY THE 3RD RESPONDENT TO THE PETITIONER.
- Exhibit P2** TRUE COPY OF THE LOAN AGREEMENT BETWEEN THE PETITIONER AND ITS SUBSIDIARY COMPANIES DATED 16.06.2016 .
- Exhibit P3** TRUE COPY OF THE LOAN AGREEMENT BETWEEN THE PETITIONER AND ITS SUBSIDIARY COMPANIES DATED 29.09.2016 .
- Exhibit P4** TRUE COPY OF THE RELEVANT PORTIONS OF THE MASTER CIRCULAR ISSUED BY THE RBI, BEARING RBI/2015-16/20 DATED 01.07.2015.
- Exhibit P5** TRUE COPY OF THE RELEVANT PORTIONS OF THE FAQS ISSUED BY RBI, DATED 12.10.2017.
- Exhibit P6** TRUE COPY OF THE RELEVANT PORTIONS OF THE INTEREST RATE POLICY ISSUED BY THE PETITIONER IN ACCORDANCE WITH THE RBI CIRCULAR DATED 26.03.2012 (GUIDELINES ON FAIR PRACTICES CODE FOR NBFCS).
- Exhibit P7** TRUE COPY OF THE VALIDITY OF NOTIFICATION 14/2017-CT DATED 01.07.2017.
- Exhibit P8** TRUE COPY OF THE VALIDITY OF CIRCULAR NO. 3/3/2017-GST DATED 05.07.2017.
- Exhibit P9** TRUE COPY OF THE CIRCULAR NO. 31/05/2018-GST DATED 09.02.2018.
- Exhibit P10** TRUE COPY OF THE AMENDED CIRCULAR NO. 169/01/2022-GST DATED 12.03.2022.



- Exhibit P11** TRUE COPY OF THE SL NO. 6 OF NOTIFICATION NO. 13/2017-CT(R) DATED 28.06.2017.
- Exhibit P12** TRUE COPY OF CONSTITUTIONAL VALIDITY OF PARA 2 OF SCHEDULE I TO THE CGST ACT DATED NIL.
- Exhibit P13** TRUE COPY OF THE CONSTITUTIONAL VALIDITY OF RULE 28 OF THE CGST RULES DATED 28.06.2017.
- Exhibit P14** TRUE COPY OF THE SECTION 3 OF THE CGST ACT DATED NIL.
- Exhibit P15** TRUE COPY OF THE SECTION 2 OF THE CGST ACT DATED NIL.
- Exhibit P16** TRUE COPY OF THE SECTION 4 OF THE CGST ACT DATED NIL.
- Exhibit P17** TRUE COPY OF THE SECTION 5 OF THE CGST ACT DATED NIL.
- Exhibit P18** TRUE COPY OF THE CORRIGENDUM NO. GSR 533(E) DATED 29.07.2019 SUBMITTED BY THE PETITIONER.
- Exhibit P19** TRUE COPY OF NOTIFICATION 2/2017-CT DATED 19.06.2017.
- Exhibit P20** TRUE COPY OF SECTION 73 OF THE CGST ACT DATED NIL.
- Exhibit P21** TRUE COPY OF SECTION 168 OF THE CGST ACT DATED NIL.
- Exhibit P22** TRUE COPY OF SECTION 7 OF THE CGST ACT DATED NIL.
- Exhibit P23** TRUE COPY OF SECTION 15 OF THE CGST ACT DATED NIL.



- Exhibit P24** TRUE COPY OF THE MINUTES OF MEETING OF THE PETITIONER DATED 15.05.2019.
- Exhibit P25** TRUE COPY OF THE INCOME TAX RETURNS OF THE PETITIONER FOR THE FINANCIAL YEAR 2017 -2018 AND 2018-2019.
- Exhibit P26** TRUE COPY OF THE CBIC CIRCULAR NO. 140/10/2020-GST DATED 10.06.2020.
- Exhibit P27** TRUE COPY OF RBI MASTER CIRCULAR GUARANTEES AND CO-ACCEPTANCES BEARING NO. RBI/2009-10/70 DATED 01.07.2009.
- Exhibit P28** TRUE COPY OF SPECIMEN LOAN AGREEMENTS WITH UN-RELATED PARTIES WHERE NO PROCESSING FEE WAS CHARGED DATED 24.12.2019.
- Exhibit P29** TRUE COPY OF SL NO. 27 OF THE NOTIFICATION NO. 12/2017-CT(R) DATED 28-06-2017.
- Exhibit P30** TRUE COPY OF THE SAID REPLY TO EXHIBIT P1 SHOW CAUSE NOTICE DATED 12.08.2022
- Exhibit P31`** TRUE COPY OF CIRCULAR NO. 204/16/2023-GST [F.NO. 20/06/22/2023-GST-CBEC], DATED 27-10-2023 ISSUED BY THE PRINCIPAL COMMISSIONER (GST)
- Exhibit P32** TRUE COPY OF THE CIRCULAR NO.218/12/2024-GST ISSUED BY THE PRINCIPAL COMMISSIONER (GST) DATED 26.06.2024.