

**IN THE CUSTOMS, EXCISE AND SERVICE TAX APPELLATE TRIBUNAL
CHENNAI**

**REGIONAL BENCH – COURT NO. III
SERVICE TAX APPEAL No.646 of 2012**

[Arising out of Order-in-Original No.LTUC/268 & 269/2012-C dated 29.08.2012 passed by Commissioner of Central Excise & Service Tax, Large Taxpayer Unit, Chennai.]

M/s. Sundaram Finance Ltd.,
No.21, Pattulas Road,
Chennai 600 002.

: Appellant

VERSUS

The Commissioner of GST & Central Excise,
Chennai North Commissionerate,
No.26/1, Mahatma Gandhi Salai,
Nungambakkam,
Chennai 600 034.

: Respondent

AND

SERVICE TAX APPEAL No.647 of 2012

[Arising out of Order-in-Original No.LTUC/268 & 269/2012-C dated 29.08.2012 passed by Commissioner of Central Excise & Service Tax, Large Taxpayer Unit, Chennai.]

M/s. Sundaram Finance Ltd.,
No.21, Pattulas Road,
Chennai 600 002.

: Appellant

VERSUS

The Commissioner of GST & Central Excise,
Chennai North Commissionerate,
No.26/1, Mahatma Gandhi Salai,
Nungambakkam,
Chennai 600 034.

: Respondent

APPEARANCE:

Shri P.C.Anand, Consultant
For the Appellant

Shri S. Balakumar, Assistant Commissioner (A.R)
For the Respondent

CORAM:

HON'BLE MS. SULEKHA BEEVI C.S., MEMBER (JUDICIAL)

HON'BLE MR. VASA SESHAGIRI RAO, MEMBER (TECHNICAL)

FINAL ORDER NO. 40067-40068 / 2023

DATE OF HEARING : 17.02.2023

DATE OF PRONOUNCEMENT:22.02.2023

Per: Ms. SULEKHA BEEVI C.S.

Brief facts of the case are that the appellant is a Non- Banking Financial Company and are engaged in the business activity of financing the purchase of commercial vehicles, cars, houses and also provide the services of Software Solutions, Business Process Outsourcing, Hire Purchase and Leasing including Equipment Leasing. They have obtained Service Tax registration for various categories of services. The appellant has a system whereby the customer who avails the loan / hire-purchase facility is permitted to pay-up ahead of the scheduled EMI, part of or the entire outstanding principal, which in financial parlance is known as "Preclosure/Foreclosure" of the loan. Appellant at the time of accepting the part payment for preclosure, in addition, also collects penal charges @ 3% on the outstanding amount. The said amount was mentioned as (Finance Charges) FC penalty in the settlement working sheet. The Department was of the view that the appellant is liable to pay service tax on the FC penalty collected by them as the same would fall under the "Banking and Other Financial Services (BOFS)". Show cause notice was issued proposing to demand service tax on such foreclosure charges along with interest and also for imposing penalties. After due process of law, the original authority confirmed the demand along with interest and imposed penalty. The appellant is thus before the Tribunal.

2. Ld. Consultant Shri P.C. Anand appeared and argued on behalf of the appellant. The details of show cause notice, period involved and the amount in each of the appeal is given in the table below :

Appeal No.	SCN No. & Date / OIO No. & Date	Period	Amount	Penalties & Interest (Rs.)
ST/646/2012	LTUC/294/2010-C dated 19.10.2010 Order in Original No.LTUC/268/2012 dt 29.8.2012	July 2001 to March 2010	3,46,64,938/-	U/s 78 3,46,64,938/- ; Interest u/s 75
ST/647/2012	LTUC/294/2010-C dated 25.05.2012 Order in Original No.LTUC/269/2012 dt 29.8.2012	April 2010 to March 2011	1,07,86,682/-	U/s 76 Minimum penalty: Interest u/s 75

3. It is submitted that the issue stands covered by the decision of the Larger Bench in the case of *Commissioner of Service Tax, Chennai Vs REPCO Home Finance Ltd.,* - 2020 (42) GSTL 104 (Tri-LB).

4. Ld. A.R Shri S. Balakumar appeared and argued for the Department.

5. The issue is whether the Foreclosure charges collected by the banks and non-banking financial companies on premature termination of loans is subject to levy of service tax under "Banking and Other Financial Services" as defined under Section 65 (12) of the Finance Act, 1994. The Larger Bench in the case of *RepcO India Ltd.* (supra) has considered the issue and held that such charges are not liable to service tax. The relevant paragraphs of the Larger Bench decision reads as under :

“47. The decision of the Tribunal in *Hudco* now needs to be examined. It concludes that the foreclosure charges would be subjected to service tax after 10 September, 2004 as the definition of “banking and other financial services” was amended under Section 65(12) of the Finance Act by including other financial services like lending in the definition. The taxable service under Section 65(105)(zm) of the Finance Act means any service provided or to be provided to any person, by a banking company or the financial institution including non-banking financial companies, or any other body corporate, in relation to “banking and other financial companies”. The definition of “banking and other financial services”, as it existed prior to 10 September, 2004, is as follows :

“banking and other financial service” means -

(a) The following services provided by a banking company or a financial institution including a non-banking financial company or any other body corporate, namely :-

- (i) financial leasing services including equipment leasing and hire purchase by a body corporate;
 - (ii) credit card services;
 - (iii) merchant banking services;
 - (iv) securities and foreign exchange (forex) broking;
 - (v) asset management including portfolio management, all forms of fund management, pension fund management, custodial, depository and trust services, but does not include cash management;
 - (vi) advisory and other auxiliary financial services including investment and portfolio research and advice, advice on merges and acquisitions and advice on corporate restructuring and strategy; and
 - (vii) provision and transfer of information and data processing;
- (b) foreign exchange broking provided by a foreign exchange broker other than those covered under sub-clause (a);

48. Section 65(12) was substituted with effect from 10 September, 2004 by adding two clauses which are as follows :

- (viii) banker to an issue services; and
- (ix) other financial services, namely, lending; issue of pay order, demand draft, cheque, letter of credit and bill of exchange; transfer of money including telegraphic transfer, mail transfer and electronic transfer; providing bank guarantee, overdraft facility, bill discounting facility, safe deposit locker, safe vaults; operation of bank accounts;

49. The Bench observed that when pre-payment is proposed, the borrower is expected to make a request which has to be considered by the banks, charges have to be worked out and informed. Thus there is an element of service involved in considering the request of the borrower for pre-payment of loan, fixing of pre-payment charges collection of the same and closure of their loan. The relevant portion of the order is reproduced below :

“10. Admittedly, the prepayment charges vary from borrower, according to the appellant themselves. Further, it is collected for premature closure of the loan and it is not the interest factor that is taken into account. It has to be noted that when a borrower makes a prepayment and therefore pays interest separately up to the date of payment, that amount is shown separately as interest and prepayment charges are not collected as interest, but collected as prepayment charges. Further even though the borrower has already borrowed the money and the process is over, when prepayment is proposed, borrower is expected to make a request which has to be considered by lender, charges worked out and informed and paid along with principal and interest up to the date of payment. Therefore, there is definitely an element of service involved in considering the request of the borrower for prepayment of loan, fixing of prepayment charges, collection of the same and closure of loan. These activities can be definitely in relation to Banking and other Financial Services, which includes lending after 10-9-2004. Further, when loans are foreclosed, the situation gives rise to the issue of asset liability mis-match for the lender since lender has to find alternative source for deployment of such funds. Prepayment charges are the charges leviable by a bank/lender to offset the cost of such finding such alternative source for deployment of fund and also intended to make exit difficult for the borrower. This shows that prepayment charges can never be considered to be the nature of interest.”

50. The decision rendered in *Small Industries (I)* (supra) was distinguished for the reason that it dealt with a period prior to 10 September, 2004.

51. It is not possible to accept the reasoning given by the Bench in *Hudco* in view of the discussions made above. The amount of damages is clearly stipulated in the contracts and no element of service is sought to have been rendered by the banks to borrowers. In fact, as noticed above, the contract has been broken by the borrowers for which the banks are entitled to claim damages. The foreclosure charges are nothing but damages which the banks are entitled to receive when the contract is broken. The amendment made in Section 65(12) of the Finance Act in the definition of “banking and other financial services” by addition of “lending” is not relevant at all for the purpose of determining whether service tax can be levied on foreclosure charges.

52. The submission of the Learned Authorised Representative of the Department that premature closure is a facility available to a borrower at a price in the same manner as a facility for availing a loan for a price and, therefore, the activity would fall within the ambit of “banking and other financial services” cannot, therefore, be accepted.

53. Thus, for all the reason stated above, it is not possible to subscribe to the view taken by the Bench of the Tribunal in *Hudco*. Service tax cannot be levied on the foreclosure charges levied by the banks and non-banking financial companies on premature termination of loans under “banking and other financial services” as defined under Section 65(12) of the Finance Act.

54. The reference is, accordingly, answered in the following terms;

“Foreclosure charges collected by the banks and non-banking financial companies on premature termination of loans are not leviable to service tax under “banking and other financial services” as defined under Section 65(12) of the Finance Act.”

6. Following the decision of the Larger Bench of the Tribunal, we are of the view that the demand cannot sustain and requires to be set aside which we hereby do. The impugned orders are set aside. The appeals are allowed with consequential relief, if any, as per law.

(pronounced in court on 22.02.2023)

Sd/-
(SULEKHA BEEVI C.S.)
MEMBER (JUDICIAL)

Sd/-
(VASA SESHAGIRI RAO)
MEMBER (TECHNICAL)

gs