



Date: 28rd June, 2016

To,
Commissioner of Commercial Tax
Government of Uttar Pradesh,
4, Vibhuti Khand
Gomti Nagar
Lucknow - 226016
Uttar Pradesh

Sub: Representation to facilitate the provision for entitlement to tax credit in respect of leasing transactions under The Uttar Pradesh Vat Act, 2008

Respected Sir,

Asset Finance Association of India (AFAI), an industry body formed with the objective of promoting leasing, factoring and other asset-backed financing entities is an initiative by the Indian Securitisation Foundation (ISF), a non-profit organization incorporated with the cause of promoting capital market instruments in the country. Some of the eminent players of the leasing industry are members to AFAI and are dedicated to the cause of promoting leasing in India. The details of AFAI, its activities and members are provided for in **Annexure I** to this representation.

The purpose of this representation is to humbly request to facilitate the provision for entitlement to tax credit in respect of leasing transactions under The Uttar Pradesh Value Added Tax Act, 2008¹ (“Act”).

Summary of the Representation

Proviso to section 2(p) of the Act, defining input tax, provides that the tax paid or payable in respect of transfer of right to use any goods shall not form part of the input tax. Consequently lessee will not be able to claim input tax credit (ITC) of the tax paid in respect of transfer of right to use.

Further, section 13 of the Act contains detailed provisions as to ITC, where under section 13(7)(c)(iii) it has been specifically provided that no provision of ITC shall be available to a dealer in respect of purchase of any goods to be provided on right to use basis.

Therefore we humbly request to facilitate the provision for entitlement to ITC in respect of leasing transactions under the Act by deleting the proviso to section 2(p) and section 13(7)(c)(iii) of the Act.

¹ http://comtax.up.nic.in/Vat_Act/UPVAT%20ACT%20Updated%20upto%20dt%2012march2015.pdf



Leasing Industry in India

The Indian leasing industry has witnessed some growth in leasing volumes since 2010 and has seen several new players venture into new asset classes after leasing in India came to a sudden halt in 1996. Leasing has found favor as some of the issues from the past resolved, corporates preferred usage of several assets over ownership, technological obsolescence also created an inclination towards appreciating usage benefits over ownership, leasing facilitated creation of new customer class, as a tool to boost sales for some asset classes and more.

While assessing the performance of the Indian leasing industry, it is noted that the leasing volumes stood at around USD 669 million² during FY 2014-2015 as opposed to USD 505 million during FY 2013-2014. The leasing industry outlines the upward trajectory motion in terms of growth. The acquisition of capital goods involve high cash outflow, thus importers opt for equipment leasing rather than buying outright. Leasing, as an alternative provides several benefits which are enumerated below:

1. Technological upgradations are suitably met with the lease form of financing. It is easy for companies to replace their worn out or obsolete machines with the leased assets.
2. Hedging of technological obsolescence helps equipment users to avoid the burdens of ownership, one of them being equipment obsolescence. Much of today's equipment incorporates technology that is rapidly changing.
3. Cashflow constraints makes leasing attractive. An outright purchase requires an immediate cash outflow, whereas in case of lease, the cash outflow are spread over years of usage of the asset. Also in case of leased assets, the ownership of the assets is retained by the leasing entity and only the usage of the assets is transferred to the end user. Therefore, in most lease cases, there is no requirement for additional collateral.

The Uttar Pradesh Value Added Tax Act 2008

The Uttar Pradesh Value Added Tax Act 2008, passed by the Government of Uttar Pradesh had come into force as on 1st January, 2008. Under the Act –

- ITC is denied to the lessee in respect of transfer of right to use any goods.
- ITC is denied to a dealer in respect of purchase of any goods to be provided on right to use basis.

The aforesaid could be substantiated as under -

- a. Section 2(ac) of the Act defines sales as under –

² The leasing volumes do not include new leasing business volumes of Indian Railway Finance Corporation a subsidiary of Indian Railways



"sale" with its grammatical variations and cognate expressions, means any transfer of property in goods (otherwise than by way of a mortgage, hypothecation, charge or pledge) by one person to another, for

cash or for deferred payment or for any other valuable consideration and includes, -

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(iv) a transfer of the right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration;

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Hence transfer of right to use goods qualifies to be a sale under the provisions of the Act.

b. Section 2(q) of the Act defines lease as under –

"lease" means any agreement or arrangement whereby the right to use any goods for any purpose is transferred by one person to another (whether or not for a specified period) for cash, deferred payment or other valuable consideration without the transfer of ownership and includes a sub-lease but does not include any transfer on hire purchase or any system of payment by instalments"

c. Section 2(r) of the Act defines lessee as any person to whom the right to use goods for any purpose is transferred under a lease.

d. Section 2(s) of the Act defines lessor as any person by whom the right to use any goods for any purpose is transferred under a lease.

e. Section 2(p) of the Act provides the definition of "input tax". The same has been reproduced as under –

(p) "input tax" in relation to a registered dealer who has purchased any goods from within the State, means the aggregate of the amounts of tax, -

i) paid or payable by such registered dealer to the registered selling dealer of such goods in respect of purchase of such goods; and

ii) paid directly to the State Government by the purchasing dealer himself in respect of purchase of such goods where such purchasing dealer is liable to pay tax under this Act on the turnover of purchase of such goods



Provided that tax paid or payable in respect of transfer of right to use any goods shall not form part of the input tax

Proviso to section 2(p) of the Act defining input tax provides that the tax paid or payable in respect of transfer of right to use any goods shall not form part of the input tax. Consequently lessee will not be able to claim ITC of the tax paid in respect of transfer of right to use as the same will not qualify as input tax.

- f. Section 13 of the Act lay down the detailed provisions as to ITC. Section 13(7) of the Act provides for circumstances under which ITC will not be allowed. The same has been reproduced as under –

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(7) Except where –

- a) purchased goods; or*
- b) manufactured goods which are manufactured by using purchased goods; or*
- c) packed goods which are packed by using or consuming purchased goods are to be sold in the course of the export of the goods out of the territory of India, no credit of any amount of input tax shall be claimed by a dealer under sub section (4) and no facility of input tax credit shall be allowed to a dealer in respect of purchase of any goods where –*

(i) sale of such goods by the dealer is exempt from payment of tax under clause (c) of section 7; or

(ii) such goods are to be used or consumed in manufacture or packing of any goods and sale of such manufactured or packed goods by the dealer is exempt from payment of tax either under clause (b) or clause (c) of section 7.

(iii) such goods are for transfer of right to use such goods."

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Section 13(7)(c)(iii) of the Act denies ITC to a dealer in respect of purchase goods to be provided on right to use basis.

While the reasons for denial of ITC benefit in case of leasing transactions under the Act are not known, we humbly request your good-self to kindly

- delete the proviso to section 2(p) of the Act so that the tax paid or payable in respect of transfer of right to use any goods forms a part of the input tax and;



- delete section 13(7)(c)(iii) of the Act so that a dealer is able to claim input tax credit in respect of purchase of any goods to be provided on right to use basis.

The other definitions relevant to explaining the position in case of availability of input tax credit for assets provided on right to use basis is provided in **Annexure – II** to this representation.

Our Representation

Given the fact that Uttar Pradesh is the third largest Indian state by economy and fourth largest Indian state by area, Uttar Pradesh has been performing well on several fronts including economic growth, infrastructure development and labour productivity. The state has seen 67.4% increase in number of the establishments between 2005 and 2013 compared to national average of 41.8%³. Between 2004-05 and 2014-15, Gross State Domestic Product (GSDP) expanded at a Compound Annual Growth Rate (CAGR) of 10.72 per cent to US\$ 161.1 billion where as the Net State Domestic Product (NSDP) expanded at a CAGR of 10.66 per cent to US\$ 142.1 billion⁴. The numbers quoted above do supplement the fact that there are robust growth opportunities available in the state. Also with the further rise in the GSDP of the state the need for capital expenditure will be on a rise.

Therefore need for having several financial products to be able to meet the capital expenditures for industries becomes quintessential to support the demand for capex. Leasing is one of the tools which facilitates use of the fixed assets and also distributes the cash outflows over a period of time. However, the extant provisions in the VAT Act pertaining to input tax credit denial in case of lease transactions makes leasing completely non-lucrative proposition for lessees and lessors in the state.

Outright purchase of assets poses several constraints, a) there is an immediate cash outflow which may not be possible for several business houses considering the tight cashflows business these days work on, b) there is a need for constant technological upgradation that throw the owned asset into redundancy and c) business houses can appreciate the need for usage of the assets more than need for owning the assets. Leasing as a product takes care of these constraints. The cash outflows are spread over the lease tenure. Lease facilitates the lessee to use the asset and pay for the usage with no obligation to own the asset at any point of time. The lease could be terminated in favour of an upgraded asset to ensure that the business is not constrained by the technological obsolescence. Therefore, lease has several merits over outright ownership and/ or acquiring the asset on loan as well.

The ITC disallowance, becomes a sunk cost and therefore puts leasing out of preference reducing prospective lessees to either purchase or avail loan facility. A sine-quo-non to a flourishing economy is availability of various financial products and how developed financial products are.

³ <http://www.thehindu.com/business/Economy/up-tops-growth-in-enterprises-jobs/article8426989.ece>

⁴ <http://www.financialexpress.com/article/economy/uttar-pradesh-likely-to-achieve-10-growth-in-fy17-assoam/43521/>



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Considering Uttar Pradesh government's vision and policy initiatives, the input tax credit denial is not helping the cause of growth and development in the state. It is, infact, working on cross purposes.

Similar ITC denial was inserted by the Maharashtra government in case of lease of passenger vehicles in the year 2013. However, this position was over-turned in the recent state Budget where the input tax credit was reinstated after recognising the criticality of survival of leasing in the segment. The amendment in the Maharashtra Vat Act reinstating input tax credit on passenger motor vehicles is briefly provided in **Annexure – III** to this representation for reference.

Similar to the Maharashtra government, we urge your goodself to consider the merits of leasing and facilitate the environment for leasing as a product to grow by doing away with the input tax credit disallowance in case of leases; thereby giving a level playing field with the other states as well.

As AFAI is dedicated to the cause of contributing to the development of the asset backed funding sector in particular, in the event of any further clarification needed, we would be happy to provide the same.

For *Asset Finance Association of India*

Sd/-

(Nidhi Bothra)
Executive Committee Member

Director
Indian Securitisation Foundation



Annexure - I

The Asset Finance Association of India is an initiative by the Indian Securitisation Foundation to bring together the stakeholders of the asset finance sector in India. The organisation is intended to promote, help, develop, protect, encourage and secure, in India, general interest of various forms of asset backed funding by acting as industry association, to organize industry events, forums, discussions to promote research, generally to take care of the interest of trade, industry and commerce, stakeholders, participants and investors in asset finance and generally to act in the best interest of the Indian asset finance sector. Primarily, the asset finance activities to be catered to by the Association include leasing, factoring, trades in receivables, etc.

The Association aims at bringing industry players on a common platform – to join their thoughts, and to provide a voice to their thoughts. The Association aims at providing a strong platform of advocacy for asset finance industry.

Some of the functions of the organisation include:

- **Advocacy:** making representation to various authorities from time to time on matters concerning the following –
 - a. Leasing
 - b. Factoring
 - c. Receivable Financing
 - d. Other forms of asset backed finance.
- **Industry forums and networking:** holding periodic conventions and educational courses.
- **Development of industry standards:** framing self-regulatory standards on disclosures, reporting, servicing reporting, DOs and DONTs for various forms of asset finance.
- **Information exchange:** on matters of common interest, collateral performance etc.

AFAI Executive Committee Members

1. Ms. Simi Thapar

Ms. Simi Thapar is a Head - Equipment Leasing and Financing Solutions - Corporate Finance at Tata Capital. Simi has 25 Years Work Experience in Financial Services across diverse industries and diverse asset and product categories. Ground experience in new business initiative, product development and in devising strategy for organic and inorganic growth of business.

2. Mr. Gautam Munish

Mr. Gautam Munish, currently serving Hewlett Packard financial services as regional sales director is a seasoned finance professional with 20 years of diverse work experience across Asset, Liability and Investment products. He has extensive experience in building and managing business from ground up, with exposure to



detailed competitive landscape analysis, compliance and regulatory adherence and evangelizing the merits of a differentiated approach to market.

3. *Mr. Sunil Badala*

Mr. Sunil Badala is a partner with the financial services tax practice of the Indian Firm of KPMG. He specializes both in domestic corporate tax and international tax and entry and exit strategies for multinationals and large domestic companies investing into/ outside India. He has a total of about 18 years of experience, including 14 years with the India Firm and has extensive experience in International and Domestic taxation, Inbound Entry Strategies for Multinationals and Outbound Structuring Strategies for large domestic companies.

4. *Mr. Shrirang Tambe*

Mr. Shrirang Tambe founder and CEO of ORIGA Leasing one of the first FinTech asset leasing companies for high growth oriented companies with philosophy of access to finance. His expertise lies in advising and nurturing growth oriented companies across financial and strategic areas.

5. *Ms. Nidhi Bothra*

Ms. Bothra is a consultant on leasing, asset backed lending, securitisation, structured finance and corporate finance and is Executive Vice President in Vinod Kothari Consultants (P) Ltd. Ms. Bothra has conducted various corporate training workshops on leasing, and has handled several consulting assignments on leasing in different markets. Nidhi has analysed state of leasing industry in several countries and writes the report on the state of leasing industry in India for several years now.

6. *Mr. Dipankar Sen*

A MBA graduate with specialisation in finance, He has over 20 years of experience in leasing and financial services and today heads the leasing portfolio for Orix in India. His experience has been in both fund based and fee based activities where he has managed the SME, Corporate and PSU segments for their leasing requirements in equipments. Under the leasing portfolio in Orix, he today manages the vehicle leasing business where company offers solutions in both dry and wet leases.



Annexure – II

DEFINITIONS

Capital Goods [Section 2(f)]

“capital goods” means any plant, machine, machinery, equipment, apparatus, tool, appliance or electrical installation used for manufacture or processing of any goods for sale by the dealer and includes:-

- (i) components, spare parts and accessories of such plant, machine, machinery, equipment, apparatus, tool, appliance or electrical installation;
- (ii) moulds and dies;
- (iii) storage tank;
- (iv) pollution control equipment;
- (v) refractory and refractory materials;
- (vi) tubes and pipes and fittings thereof,
- (vii) lab equipments, instruments and accessories,
- (viii) machinery, loader, equipment for lifting or moving goods within factory premises,
or
- (ix) generator and boiler

used in manufacture of goods for sale by him but for the purpose of section 13, does not include:-

- (i) air-conditioning units or air conditioners, refrigerators, air coolers, fans, and air circulators if not connected with manufacturing process;
- (ii) an automobile including commercial vehicles, and two or three wheelers, and parts, components and accessories for repair and maintenance thereof;
- (iii) goods purchased and accounted for in business but utilised for the purpose of providing facility to the employees.
- (iv) vehicle used for transporting goods or passengers or both;
- (v) capital goods used in the execution of a works contract; and
- (vi) deleted w.e.f. 16.07.2008

Dealer [Section 2(h)]

"dealer" means any person who carries on in Uttar Pradesh (whether regularly or otherwise) the business of buying, selling, supplying or distributing goods directly or indirectly, for cash or deferred payment or for commission, remuneration or other valuable consideration and includes, -



(viii) any person who carries on the business of transfer of the right to use any goods for any purpose (whether or not for a specified period) for cash or for deferred payment or other valuable consideration;

Input Tax [Section 2(p)]

(p) “input tax” in relation to a registered dealer who has purchased any goods from within the State, means the aggregate of the amounts of tax, -

(i) paid or payable by such registered dealer to the registered selling dealer of such goods in respect of purchase of such goods; and

(ii) paid directly to the State Government by the purchasing dealer himself in respect of purchase of such goods where such purchasing dealer is liable to pay tax under this Act on the turnover of purchase of such goods.

Provided that tax paid or payable in respect of transfer of right to use any goods shall not form part of the input tax.

Lease [Section 2(q)]

"lease" means any agreement or arrangement whereby the right to use any goods for any purpose is transferred by one person to another (whether or not for a specified period) for cash, deferred payment or other valuable consideration without the transfer of ownership and includes a sub-lease but does not include any transfer on hire purchase or any system of payment by installments.

Lessee [Section 2(r)]

"lessee" means any person to whom the right to use goods for any purpose is transferred under a lease.

Lease [Section 2(s)]

"lessor" means any person by whom the right to use any goods for any purpose is transferred under a lease.

Sale [Section 2(ac)]

"sale" with its grammatical variations and cognate expressions, means any transfer of property in goods (otherwise than by way of a mortgage, hypothecation, charge or pledge) by one person to another, for cash or for deferred payment or for any other valuable consideration and includes, -

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(iv) a transfer of the right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration;

Sale price [Section 2(ad)]



"sale price" means the amount payable to a dealer as consideration for the sale of any goods, less any sum allowed as cash discount according to the practice normally prevailing in the trade, but inclusive of any sum charged for anything done by the dealer in respect of goods at the time of or before the delivery of such goods, other than cost of outward freight or delivery or cost of installation in cases where such cost is separately charged;

Explanation:-

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(iv) In respect of transfer of right to use goods, any goods for any purpose (whether or not for a specified period) sale price means the valuable consideration received or receivable in respect of such transfer of right to use goods but does not include any sum payable as a penalty or as compensation or damages for breach of contract.

Input Tax Credit [Section 13]

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(7) Except where-

(a) purchased goods; or

(b) manufactured goods which are manufactured by using purchased goods; or

(c) packed goods which are packed by using or consuming purchased goods are to be sold in the course of the export of the goods out of the territory of India, no credit of any amount of input tax shall be claimed by a dealer under sub section (4) and no facility of input tax credit shall be allowed to a dealer in respect of purchase of any goods where -

(i) sale of such goods by the dealer is exempt from payment of tax under clause (c) of section 7; or

(ii) such goods are to be used or consumed in manufacture or packing of any goods and sale of such manufactured or packed goods by the dealer is exempt from payment of tax either under clause (b) or clause (c) of section 7.

(iii) **such goods are for transfer of right to use such goods.**

Schedule II Part A⁵ (List of goods taxed at 4%)

Sr. No. 3. All intangible goods like copyright, patent, rep. license etc; **Transfer of right to use of goods**

⁵ http://comtax.up.nic.in/Vat_Act/UPVAT%20SCHEDULE%20Updated%20upto%20dt%2012-03-2015.pdf



Annexure – III

In the erstwhile Maharashtra Vat Rules, 2005⁶ under Rule 54(a) set-off was admissible to the claimant who was engaged in the business of transferring the right to use of “motor vehicles (not being goods vehicles)”

As per the Notification no. STR- 1506/CR-38/Taxation-1⁷ dated 8th September, 2006 the words “not being good vehicles” was substituted by the word “passenger vehicles” for better understanding.

However, as per the Notification no. VAT 1513/CR 61/Taxation.-1⁸ dated 21st May 2013 whereby set-off which was admissible on transfer of right to use the vehicle was removed with effect from 1st May, 2013 and thereby the set-off was allowed to dealer who was in the business of hiring of vehicles.

This notification caused a dent in the leasing market involved in the transfer of use of the passenger vehicles and as such a reinstatement of this notification was urgently required. This issue was dealt in the Maharashtra Budget 2016-17 and as per Para 6 of Part II of the Maharashtra Budget⁹ speech for FY 2016-17 made on 18th March, 2016 made changes to set-off rules, which provided for restoring the ITC benefit in case of lease of passenger motor vehicles

The text from the budget can be read as follows:

"Passenger motor vehicles are not eligible for set-off even if leased. I now propose that set-off on passenger motor vehicles will be available to the extent of output tax on lease of such vehicles."

Accordingly, Rule 53 of Maharashtra Value Added Tax Rules, 2005¹⁰ has been amended and a new sub-rule (11) had been inserted with effect from 1st April, 2016.

The said sub-rule is reproduced below:

“(11) (a) If the claimant dealer is engaged in the business of transferring the right to use (whether or not for a specified period) for any purpose, of passenger motor vehicles, then he shall be entitled to claim set-off of tax paid on the purchase of such motor vehicles only to the extent of tax payable on such transfer of right to use;

(b) the set off as determined under clause (a) in respect of the such vehicles shall be claimed in the period in which such right to use has been transferred by the claimant dealer.”

⁶ Read more at: http://www.raoemmar.com/assets/4e330a92-92d1-4a6e-987e-2e3493a042e0/files/docs/VAT/Maharashtra/maharashtra_vat_rules_2005.pdf

⁷ Read more at: <http://www.steasy.com/Notification/CR38%20080906%20AMEND%20RULE.pdf>

⁸ Read more at:

http://mahavat.gov.in/Mahavat/MyFold/DOWNLOADS/NOTIFICATIONS/KNOW_NOTIFI_MVAT/KNOW_NOTIFI_MVAT_06_03_13_5_37_22PM.pdf

⁹ Read more at: https://www.maharashtra.gov.in/PDF/Budget_2016_English_Part_II.pdf

¹⁰ Read more at:

http://www.mahavat.gov.in/Mahavat/MyFold/DOWNLOADS/NOTIFICATIONS/KNOW_NOTIFI_MVAT/KNOW_NOTIFI_MVAT_04_06_16_11_36_20AM.pdf



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Therefore, as per the above amendment the dealer can now set-off the tax paid on the purchase of passenger motor vehicles to the extent of tax paid on the lease rental of such passenger motor vehicle. Hence, the above amendment has brought a cheer in the leasing industry dealing in the passenger motor vehicles sector in Maharashtra.