

**WITHHOLDING TAX REQUIREMENT ON INTEREST PAID TO
NBFCs UNDER SECTION 194A**

1. Background

- 1.1 As per section 194A of the Act, any person making payment of interest is required to deduct tax at source ('TDS'). There are certain exemptions given under this section wherein the person making payment to various institutions like Banking Company, Life Insurance Companies and UTI etc., is not required to deduct TDS. Accordingly, any person making payment of interest to Banks is not required to deduct tax.
- 1.2 However, no such exemption has been provided to NBFCs from the applicability of section 194A. Accordingly, tax is required to be deducted at the rate of 10 percent from interest paid to NBFCs. This creates severe cash flow constraints since NBFCs operate on a thin spread/ margin on interest which at times is even lesser than the TDS on the gross interest. Further, due to enormous transactions, NBFCs have to face severe administrative hardship in terms of collection of TDS certificates from their thousands of customers.
- 1.3 In this regard, we wish to reiterate that NBFCs are in similar nature of business as that of Banks. Therefore, payment of interest to NBFCs should be excluded from the purview of provisions of Section 194A of the Act and tax collections through NBFCs should be made by way of advance tax. This will provide level playing field to NBFCs similar to banking companies and other public financial institution etc., which are exempt from the purview of this Section.

2. Our request / recommendation

- 2.1 In light of the above, an amendment is requested to be made in the section 194A(3)(iii) of the Act, which provides no withholding of taxes is required to made payment to Banking company, Life insurance companies etc., to include the “Non- Banking Financial Company” along with such other institutions.
- 2.2 Once the aforesaid amendment is made, section 194A(3)(iii) shall read as follows:

To such income credited to or paid to...

- (a) Any banking company to which the Banking Regulation Act, 1949 (10 of 1949), applies, or any co-operative society engaged in carrying on the business of banking (including a co-operative land mortgage bank), or*
- (b) Any financial corporation established by or under a central, state or provincial Act, or*
- (c) The Life Insurance Corporation of India established under the Life Insurance Corporation Act, 1956 (31 of 1956), or*
- (d) The Unit Trust of India established under the Unit Trust of India Act, 1963 (52 of 1963), or*
- (e) Any company or co-operative society carrying on the business of insurance, or*
- (f) Any Non- Banking Financial Company as defined under section 45-I (f) of the Reserve Bank of India Act, 1934 (2 of 1934).***
- (g) Such other institution, association or body [or class of association or bodies] which the central government may for reasons to be recorded in writing, notify in this behalf in the Official Gazette.*

In light of above discussion, we humbly request that the aforesaid suggestion/recommendation should be considered and accordingly amendment should be made in section 194A (iii) of the Act, by way of a notification.
