



Waiver of loan availed for acquiring capital asset is taxable as business income

Background

Recently, the Madras High Court in the case of Ramaniyam Homes (P.) Ltd.¹ (the taxpayer) held that the waiver of a loan availed for acquiring capital asset would amount to acquiring a benefit or perquisite and such benefit or perquisite is arising from the business of the taxpayer. Therefore, such waiver of loan is taxable as business income under Section 28(iv) of the Income-tax Act, 1961 (the Act).

Facts of the case

- During the year under consideration, the taxpayer availed a term loan from the bank for the purchase of the capital asset. Due to some financial difficulties, the taxpayer unable to repay the term loan.
- The bank mooted a proposal for a one-time settlement. As per the one-time settlement scheme, the loan outstanding was waived by the bank. The taxpayer claimed that the waiver of loan and interest is a capital receipt and excluded the same while computing taxable income.

- The Assessing Officer (AO) held that waiver of term loan by the bank under the one-time settlement scheme is income under Section 28(iv)² of the Act.
- The Commissioner of Income-tax (Appeals) [CIT(A)] followed the decision of Iskraemeco Regent Limited³ and held that Section 28(iv) is not applicable in the cases involving waiver of principal amounts of loans. The Income-tax Appellate Tribunal (the Tribunal) upheld the order of the CIT(A).

High Court's ruling

- On a perusal of the definition of income under Section 28(iv) it has been observed that income chargeable to income-tax under the head 'profits and gains of business or profession' is 'the value of any benefit or perquisite, whether convertible into money or not, arising from business or the exercise of a profession'. Therefore, it is not the actual receipt of money, but the receipt of a benefit or perquisite, which has a monetary value, whether such benefit or perquisite is convertible into money or not, covered by Section 28(iv) of the Act.

¹ CIT v. Ramaniyam Homes (P.) Ltd. [2016] 68 taxmann.com 289 (Mad)

² The value of any benefit or perquisite, whether convertible into money or not, arising from business or exercise of a profession shall be chargeable to income-tax under the head 'profits and gains of business or profession'

³ Iskraemeco Regent Limited v. CIT [2011] 196 Taxman 103 (Mad)

- It has been observed that where a gift voucher is issued, enabling the holder of the voucher to have dinner in a restaurant, it is a benefit or perquisite, which has a monetary value. If the holder of the voucher is entitled to transfer it to someone else for a monetary consideration, it becomes a perquisite convertible into money. However, irrespective of whether it is convertible into money or not, it should have a monetary value so as to attract Section 28(iv) of the Act.
- There may be cases where an incentive is granted by the supplier, waiving a portion of the sale price or granting a rebate or discount of a portion of the price to be paid, when the payments scheduled over a period of time, are made promptly. In such cases, the prompt payment of money itself brings a benefit in the form of an incentive or a rebate or a discount in the price of the product.
- In the present case, the decision of Iskraemeco Regent Limited relied on by the CIT(A) and the Tribunal for the non-applicability of Section 28(iv) of the Act does not apply in the light of the express language of Section 28(iv) of the Act.
- In various decisions⁴, it has been held that if the loan had been taken for acquiring the capital asset, waiver thereof would not amount to any income exigible to tax. However, if the loan was for trading purpose and was treated as such from the beginning in the books of account, the waiver thereof may result in the income more so when it was transferred to the profit and loss account.
- It has been observed that the waiver of a portion of the loan would certainly tantamount to the value of a benefit. This benefit may not arise from ‘the business’ of the taxpayer. However, it certainly arises from ‘business’. The absence of the prefix ‘the’ to the word ‘business’ makes a world of difference. In so far as accounting practices are concerned, no such distinction exists.
- When the loan amount borrowed for acquiring an asset gets wiped off by repayment, two entries are made in the books of account, one in the profit and loss account where payments are entered and another in the balance sheet where the amount of unrepaid loan is reflected on the side of the liability. However, when a portion of the loan is reduced, not by repayment, but by the lender writing it off, only one entry gets into the books, as a natural entry. A double entry system of accounting will not permit of one entry.
- Therefore, when a portion of the loan is waived, the total amount of loan shown on the liabilities side of the balance sheet is reduced, and the amount shown as capital reserves is increased to the extent of waiver. Alternatively, the amount representing the waived portion of the loan is shown as a capital receipt in the profit and loss account itself. These aspects have not been considered in Iskraemeco Regent Ltd.

Our comments

The issue with respect to taxability of the benefit obtained on remission of loan liability has been a subject matter of debate before the courts.

In the present case, the High Court has held that the waiver of a loan availed for acquiring capital asset would amount to acquiring a benefit or perquisite, and such benefit or perquisite is arising from the business of the taxpayer. Therefore, such waiver of loan is taxable under Section 28(iv) of the Act. The High Court observed that it is not the actual receipt of money, but the receipt of a benefit or perquisite, which has a monetary value, whether such benefit or perquisite is convertible into money or not, which is covered under Section 28(iv) of the Act.

⁴ Solid Containers Limited v. DCIT [2009] 308 ITR 417 (Bom), Mahindra & Mahindra Limited v. CIT [2003] 261 ITR 501 (Bom), Logitronics P Ltd. v. CIT [2011] 333 ITR 386 (Del), Rollatainers Ltd. v. CIT [2011] 339 ITR 54 (Del)

www.kpmg.com/in

Ahmedabad

Commerce House V, 9th Floor,
902 & 903, Near Vodafone House,
Corporate Road,
Prahlad Nagar,
Ahmedabad – 380 051
Tel: +91 79 4040 2200
Fax: +91 79 4040 2244

Bengaluru

Maruthi Info-Tech Centre
11-12/1, Inner Ring Road
Koramangala, Bangalore 560 071
Tel: +91 80 3980 6000
Fax: +91 80 3980 6999

Chandigarh

SCO 22-23 (1st Floor)
Sector 8C, Madhya Marg
Chandigarh 160 009
Tel: +91 172 393 5777/781
Fax: +91 172 393 5780

Chennai

No.10, Mahatma Gandhi Road
Nungambakkam
Chennai 600 034
Tel: +91 44 3914 5000
Fax: +91 44 3914 5999

Delhi

Building No.10, 8th Floor
DLF Cyber City, Phase II
Gurgaon, Haryana 122 002
Tel: +91 124 307 4000
Fax: +91 124 254 9101

Hyderabad

8-2-618/2
Reliance Humsafar, 4th Floor
Road No.11, Banjara Hills
Hyderabad 500 034
Tel: +91 40 3046 5000
Fax: +91 40 3046 5299

Kochi

Syama Business Center
3rd Floor, NH By Pass Road,
Vytilla, Kochi – 682019
Tel: +91 484 302 7000
Fax: +91 484 302 7001

Kolkata

Unit No. 603 – 604,
6th Floor, Tower – 1,
Godrej Waterside,
Sector – V, Salt Lake,
Kolkata 700 091
Tel: +91 33 44034000
Fax: +91 33 44034199

Mumbai

Lodha Excelus, Apollo Mills
N. M. Joshi Marg
Mahalaxmi, Mumbai 400 011
Tel: +91 22 3989 6000
Fax: +91 22 3983 6000

Noida

6th Floor, Tower A
Advant Navis Business Park
Plot No. 07, Sector 142
Noida Express Way
Noida 201 305
Tel: +91 0120 386 8000
Fax: +91 0120 386 8999

Pune

703, Godrej Castlemaine
Bund Garden
Pune 411 001
Tel: +91 20 3050 4000
Fax: +91 20 3050 4010

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