Bajaj Finance Limited (Appellant), appealing against Advance Ruling Order No. GST-ARA-22/2018-19/B-85 dated 06.08.2018 of the Maharashtra AAR

Appellate Authority for Advance Ruling — Maharashtra

ORDER NO. MAH/AAAR/SS-RJ/24/2018-19, Date- 14.03.2019 Dated **14.03.2019**

Q Questions Before the Authority

- Whether penal interest collected on delayed EMI is to be treated as 'interest' for exemption under Sr. No. 27 of Notification No. 12/2017-Central Tax (Rate) dated 28.06.2017, Sr. No. 27 of Maharashtra State Notification No. 12/2017-State Tax (Rate) dated 29.06.2017, and Sr. No. 28 of Notification No. 9/2017-Integrated Tax (Rate) dated 28.06.2017?
- If the answer to the above is negative, whether the activity of collecting penal interest by the Appellant would amount to a taxable supply under the GST regime?

F Facts

The Appellant is an NBFC that lends to customers for auto loans, loans against property, personal loans and consumer durable loans, with repayment by EMI. Where a borrower pays an EMI late, the loan agreement lets the Appellant levy a 'penal charge' or 'late payment penalty' on the overdue amount, generally 2% to 4% per month depending on the product, with the agreement capping it at 3% per month. The Appellant treats this as additional interest and sought an advance ruling on whether it is exempt or taxable.

H Ruling

Whether penal interest on delayed EMI is 'interest' exempt under Sr. No. 27 of Notification 12/2017-CT (Rate), Sr. No. 27 of Maharashtra notification 12/2017-ST (Rate) and Sr. No. 28 of Notification 9/2017-IT (Rate)	**No. Penal charges are not exempt interest.**	Clause 2(zk) defines 'interest' as payable in respect of moneys borrowed and expressly excludes other charges. The order treats the charge as penalty or penal charges, not interest.
Whether collecting penal interest is a taxable supply under the GST regime	**Yes. It is a supply of services under entry 5(e) of Schedule II to the CGST Act.**	The order does not state a GST rate, SAC code or taxable value. The answer rests on tolerance of the delay for consideration.

The Appellate Authority dismissed the appeal and upheld the AAR's ruling. It held that the penal charges are penalty or penal charges, not 'interest' as defined in clause 2(zk) of the exemption notification, so they do not qualify for the Sr. No. 27 exemption. It further held that collecting them is a supply of services under entry 5(e) of Schedule II to the CGST Act, because the lender tolerates the borrower's delay in payment in return for the charge, and that such supply attracts GST.

Prepared as a reading aid. Where this summary and the original order differ, the order governs.

R Reasoning

The Authority held that clause 2(zk) of the exemption notification is restrictive and does not extend to 'other charges' in respect of borrowed money, so penal charges fall outside the exemption. It treated the 'penalty' label in the loan agreement as relevant but not decisive, and looked to the substance: the charge is payable only on default and is recovered in place of enforcing the loan remedies. It read entry 5(e) of Schedule II, which covers agreeing to the obligation to tolerate an act or situation, as applying to the lender's tolerance of the delay, and it treated the charge as consideration under section 2(31). It rejected the Appellant's reliance on section 73 and 74 of the Contract Act, on foreign rulings, and on the contention that 'obligation' requires a reciprocal legal duty.

P Provisions Relied On

Section 7(1)(a) of the CGST Act	Section 2(31) of the CGST Act (definition of 'consideration')
Section 15(2)(d) of the CGST Act	Schedule II, entry 5(e) of the CGST Act

- Entry 27 of Notification No. 12/2017-Central Tax (Rate) dated 28.06.2017
- Clause 2(zk) of the exemption notification (definition of 'interest')
- Sections 73 and 74 of the Indian Contract Act, 1872 (as argued by the Appellant)
- Section 2(a) of the Specific Relief Act, 1963 (definition of 'obligation', as cited by the Appellant)

! For the Practitioner

Lenders charging penal or late-payment charges on EMI defaults can take this order as the Maharashtra appellate view that such charges fall outside the interest exemption and are taxable under entry 5(e). It does not decide the GST rate, the taxable value, or the treatment of charges in other states. As a State appellate order it binds the parties, but other forums are not bound by it. Practitioners should check whether it was challenged in a higher forum before relying on it.

Source

Summary prepared from the published order, which is a scanned document. It is a reading aid and not the authority: where the two differ, the order governs. Verify every provision against the original before relying on it.

Original order: www.gstcouncil.gov.in -> mah_aaar_ss-rj_24_2018-19.pdf

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Pune (HQ)
RTC Silver, B4-708, Sai Satyam Park, Wagholi, Pune, Maharashtra 412207

Mumbai
104, Rajshila Building, 597 J.S.S. Road, Marine Lines, Mumbai 400002

Delhi
3rd Floor, B-6/154-155, Sector 5, Rohini, Delhi 110085

Gurugram
Pioneer Urban Square, B109, Golf Course Ext Road, Sector 62, Gurugram…

Ahmedabad
Phoenix Tower, 1107, near Commerce Six Road, Drive In Road, Navrangp…

Talk to us: **+91 94594 56700** | sales@patronaccounting.com | patronaccounting.com

Patron Accounting LLP