



Global Business Tax Alert

Sharp Insights

The Delhi Tribunal in the case of Stryker Global Technology Center (P.) Ltd. vs. Assistant Commissioner of Income-tax (ITA No. 149/Delhi/2013), held that the rent equalization reserve, which was debited to the profit and loss account is not in accordance with Accounting Standard 19. The reserve be added back while computing book profit under section 115JB of the Income-tax Act, 1961 ('the Act'), the Tribunal said.

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Background

- Stryker Global Technology Center (P.) Ltd. ('the taxpayer') occupied a premise on lease along with the right to use common facilities. The said lease was for three years with an option to renew for another two consecutive terms of three years.
- The taxpayer debited rent equalization reserve to the profit and loss account based on straight lining of lease rentals payable by the taxpayer under an operating lease occupied by it during the financial year under consideration, and in accordance with Accounting Standard 19 ('AS 19'): 'Accounting for Leases'. The said reserve was created on the basis of 9 years lease period.
- During the assessment proceedings, the taxpayer submitted that such reserve was inadvertently not added back while computing the taxable income under the normal provisions of the Act, due to lack of clarity on its allowability under the normal provisions of the Act. Accordingly, the taxpayer offered the amount debited as rent equalization reserve, in its Profit and Loss Account, during the financial year under consideration, to be taxed under the normal provisions of the Act.
- The taxpayer, however, did not add back the same while computing the book profit as per Explanation 1 of clause (b) and (c) to section 115JB of the Act.
- The Assessing Officer ('AO'), however, added back the amount of reserve debited in the Profit and Loss account for computing the book profits of the taxpayer. The Dispute Resolution Panel ('DRP') confirmed the actions of the AO and accordingly, the AO gave effect to the DRP directions.
- Aggrieved by the directions of the DRP, the taxpayer preferred to file an appeal with the Tribunal.

Ruling of the Tribunal

- The Tribunal discussed the scope of AS 19 and the classification of leases for the purpose of AS 19.
- The Tribunal observed that the main object of AS 19 is to deal with leases concerning movable assets and it specifically excludes lease agreements to use lands. Accordingly, AS 19 is not applicable to lease of immovable property.
- On that basis the Tribunal held that the AO rightly added back the rent equalization reserve, debited to Profit and Loss account, while computing the book profit for the purposes of section 115JB of the Act.
- Moreover, the taxpayer has added back this reserve for purposes of computation of total income under the normal provisions of the Act. Therefore, the stand of the taxpayer of not adding back while computing book profits is contradictory.
- Accordingly, the Tribunal dismissed the appeal filed by the taxpayer.

Conclusion

The Tribunal held that rent equalization reserve debited to Profit and Loss account, which is not in accordance with AS 19, should be added while computing book profits under section 115JB of the Act.

The taxpayer may accordingly examine whether the provision or reserve created, are in accordance with the Accounting Standard or not while computing book profit.

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Contacts

Ahmedabad

19th Floor, Shapath - V
SG Highway,
Ahmedabad – 380 015.
Tel: + 91 (079) 6682 7300
Fax: + 91 (079) 6682 7400

Coimbatore

Shanmugha Manram
41, Race Course,
Coimbatore
Tamil Nadu - 641018
Tel: + 91 (0422) 439 2801
Fax: +91 (0422) 222 3615

Kolkata

Bengal Intelligent Park Building
Alpha, 1st floor, Block EP and GP
Sector V, Salt Lake Electronics
Complex,
Kolkata - 700 091.
Tel : + 91 (033) 6612 1000
Fax : + 91 (033) 6612 1001

Bangalore

Deloitte Centre, Anchorage II,
100/2, Richmond Road,
Bangalore 560 025.
Tel: +91 (080) 6627 6000
Fax: +91 (080) 6627 6010

Delhi/Gurgaon

Building 10,
Tower B, 7th Floor,
DLF Cyber City,
Gurgaon 122 002
Tel : +91 (0124) 679 2000
Fax : + 91 (0124) 679 2012

Mumbai

Indiabulls Finance Centre,
Tower 3, 28th Floor,
Elphinstone Mill Compound,
Senapati Bapat Marg, Elphinstone
(W),
Mumbai – 400013
Tel: + 91 (022) 6185 4000
Fax: + 91 (022) 6185 4101

Chennai

No.52, Venkatanarayana Road,
7th Floor, ASV N Ramana Tower,
T-Nagar,
Chennai 600 017.
Tel: +91 (044) 6688 5000
Fax: +91 (044) 6688 5050

Hyderabad

1-8-384 and 385, 3rd Floor,
Gowra Grand S.P.Road,
Begumpet,
Secunderabad – 500 003.
Tel: +91 (040) 6603 2600
Fax: +91 (040) 6603 2714

Pune

106, B-Wing, 7th Floor,
ICC Trade Tower,
Senapati Bapat Road,
Pune – 411 016.
Tel: + 91 (020) 6624 4600
Fax: +91 (020) 6624 4605



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