



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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