

#### **Query No. 4**

**Subject:** *Accounting for GST component paid on lease payment under Ind AS 116, 'Leases'.<sup>1</sup>*

#### **A. Facts of the Case**

1. A company (hereinafter referred to as 'the Company') was incorporated on 27.09.2004 as a joint venture of O Ltd. (50%), I Ltd. (49.50%) and Government of Tripura (GoT) (0.50%). The Company is a deemed public sector undertaking (PSU) having 726.63 MW of gas based power plant in the State of Tripura and having corporate office at Delhi.

2. The first block (363.3 MW) of the power plant was declared under commercial operation from 4<sup>th</sup> January 2014 and the second block (363.3 MW) of the two blocks was declared under commercial operation from 24<sup>th</sup> March 2015.

3. B Ltd. was the Engineering, Procurement, and Construction (EPC) contractor for setting up of the power plant. Subsequently, in April 2015, I Fund (managed by GP LLP\*, which is a wholly owned subsidiary of GM LLC (USA)) became an investor in the Company by acquiring 23.5% of the equity stake.

(\*Status converted to GP Pvt. Ltd. w.e.f. 3<sup>rd</sup> January 2022.)

4. GI Ltd., a public sector undertaking (PSU) under the Ministry of Petroleum and Natural Gas (MoPNG) has acquired the 26% equity stake in the Company on 04<sup>th</sup> January 2022 from I Ltd. group companies. Accordingly, w.e.f. 04.01.2022, GI Ltd. has become shareholder of the Company replacing I Ltd. group companies.

5. The setting up of the power plant has helped in transforming the power scenario of the entire North-Eastern region of the country and has assisted in catalysing rapid economic development of the region. The generation project combined with linked transmission project and upstream gas supply project has brought in investments to the tune of Rs. 10,000 crores in the region.

6. The Company has taken corporate office premises at Delhi on lease from O Ltd. (the lessor) at a monthly rent of Rs. 17.80 lakhs plus Goods and Services Tax (GST) at the rate of 18% thereon for a period of 01<sup>st</sup> November 2023 to 31<sup>st</sup> October 2026 with 5% annual escalation in rent. The said premises (Scope Minar) is maintained by Maintenance Management Organisation (MMO) of the Scope Minar (Standing Conference of Public Enterprises (SCOPE)).

7. In addition to monthly rent, the Company is also required to pay electricity and maintenance charges including ground rent payable to SCOPE at actuals on pro rata basis to the lessor. Further, the Company has also paid interest-free security deposit amount of Rs. 53.40 lakhs for corporate office taken on lease and such security deposit amount will be refunded after completion of lease term. The lease agreement could be further renewed after 3 years (i.e. after 31<sup>st</sup> October 2026) on the terms and conditions agreed upon between lessor and lessee.

8. As per paragraph 22 of Indian Accounting Standard (Ind AS) 116, 'Leases', the Company has recognised right of use (RoU) asset and lease liability in its books of account

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<sup>1</sup> Opinion finalised by the Committee on 28.4.2025.

against lease amount of Rs. 17.80 lakhs per month plus GST component thereon. The right of use (RoU) asset recognised for the same is being amortised as per depreciation policy of the Company for same class of assets and monthly lease repayments are bifurcated between lease liability and interest payment on lease payments.

9. The Company is subject to annual audit by the Comptroller and Auditor General of India (CAG) with effect from financial year (F.Y.) 2022-23 after acquisition of 26% share capital by GI Ltd. in addition to statutory audit as per the provisions of the Companies Act, 2013.

During supplementary audit for F.Y. 2023-24, CAG team has made observation on the measurement of right of use (RoU) asset as per lease provisions of Ind AS 116 in the books of account of the Company. The Company has considered the monthly lease rent payable including GST to calculate present value of minimum lease payments to recognise the right of use (RoU) asset and corresponding lease liability.

CAG team referred the Educational Material on Ind AS 116 issued in January 2020 by the erstwhile Ind AS Implementation Committee of the Institute of Chartered Accountants of India (ICAI) on the treatment of goods and service tax (GST) which states that GST should not be considered as lease payment.

The relevant question is mentioned below:

“Entity X (lessee) enters into an agreement with Entity Y to lease an entire floor of a building for a period of 10 years. The annual lease payments are fixed at INR 30,00,000 and are required to be paid in advance. In addition, Entity X shall pay Goods and Services Tax (GST) at 18% to Entity Y, who will remit the tax to the applicable government. GST is non-refundable and Entity X cannot claim the input tax credit for the GST payment.

Whether the payment of GST is considered as a part of consideration paid by Entity X? How will Entity X account for the GST payments?

### **Response**

Paragraph 17 of Ind AS 116 states as follows:

“17 For a contract that contains a lease component and one or more additional lease or non-lease components, a lessor shall allocate the consideration in the contract applying paragraphs 73–90 of Ind AS 115.”

Section 9(1) of the Central Goods and Services Tax Act, 2017 provides that, “*Subject to the provisions of sub-section (2), there shall be levied a tax called the central goods and services tax (CGST) on all intra-state supplies of goods or services or both, except on the supply of alcoholic liquor for human consumption, on the value determined ..... and collected in such manner as may be prescribed and shall be paid by the taxable person*”. Similar provisions are also included for State Goods and Services Tax Act (SGST), Integrated Goods and Services Tax Act (IGST) and Union Territory Goods and Services Tax Act (UGST).”

In accordance with the above, the incidence of GST (i.e. CGST/SGST/IGST/ UGST) is on supply of goods or services and it is recovered from the customer.

Amounts collected on behalf of third parties such as sales taxes, goods and services taxes and value added taxes are not economic benefits which flow to the entity. Therefore, they are excluded from revenue.

On the similar guidance, GST is a consumption based tax which is the liability of the lessee towards the Government. Although the same is paid by the lessee to the lessor, it cannot be considered as 'lease payment' since it is paid to the government and the lessor is merely acting as a collection agent. Therefore, GST, whether or not refundable, would not be included in the measurement of the lease liability or right-of-use asset.

Accordingly, Entity X will calculate lease liability based on the lease payments amounting to INR 30,00,000 per annum, i.e., excluding GST.

GST would be charged to the profit or loss when the underlying transaction occurs if input credit is not available. However, if GST is refundable/input credit is available, then GST is recognised as an asset.”

*Company's point of view:*

10. As per paragraph 22 of Ind AS 116, 'Leases', the Company has classified Delhi office premises lease agreement as lease under the provisions of Ind AS 116 and recognised 'Right of Use asset (RoU)' and 'Lease liability'. The Company has considered GST of 18% payable on monthly lease payment as part of lease payment amount and discounted the gross amount while calculating the right of use asset (RoU) and lease liability on effective date.

11. The Company is an electricity generation company and sale of electrical energy is exempted from the purview of GST. The Company does not recognise GST inputs credit in its books of account related to electricity related transactions.

12. The Company has considered GST on lease payment as expense and discounted the gross lease payment including GST component thereon while calculating the right of use (RoU) asset and lease liability because such GST component is not recoverable as the Company's output services are exempt under GST. Further, in case, if only lease payment excluding GST amount of 18% thereon is discounted and GST of 18% will be debited to Statement of Profit and Loss (P&L) under the head lease expense, it would give the wrong picture to the investor regarding existence of additional leases, whereas the accounting standard provides that only short-term and low value leases are to be expensed in the P&L.

13. According to the querist, the Educational Material referred by CAG team is recommendatory in nature and such accounting treatment mentioned in the FAQ of Educational Material cannot be taken as the basis.

**B. Query**

14. In view of the above, the opinion of the Expert Advisory Committee is sought as to whether GST component paid on lease payment can be a part of right of use (RoU) asset and lease liability from the lessee's perspective while calculating the present value of right of use

(RoU) asset and lease liability in cases where the Company's output services are exempt from GST provisions.

### C. Points considered by the Committee

15. The Committee notes that the basic issue raised in the query relates to whether GST component on lease payment should be included in the value of right of use (RoU) asset and lease liability recognised for office premises taken on lease. Therefore, the Committee has examined this issue only and has not examined any other issue that may arise from the Facts of the Case, such as, accounting for annual escalation in the lease rent, accounting for ground rent, electricity charges, maintenance charges etc. being paid by the Company, accounting for interest-free security deposit submitted by the Company, accounting in the books of lessor, amortisation of RoU asset, computation of lease term, accounting for monthly lease payments and its bifurcation between lease liability and interest payment, related party disclosures as per Ind AS 24, 'Related Party Disclosures', disclosures under Ind AS 116, etc. The Committee has examined the issue only from an accounting perspective and has not examined the regulatory or legal classification and implications, including those arising under Goods and Services Tax Act and Income-tax Act. The Committee also wishes to mention that the opinion expressed hereinafter is in the context of Indian Accounting Standards, notified under the Companies (Indian Accounting Standards) Rules, 2015 as amended or revised from time to time.

At the outset, the Committee notes that the Company obtained office premises on lease from O Ltd., who is one of the investors in the Company. In this regard, the Committee presumes that in the extant case, lease terms are at market terms and therefore, the Committee has not analysed the impact of any off-market terms on lease accounting.

16. In the context of the issue raised, the Committee notes the following paragraphs from the Ind AS 116, 'Leases':

**“23 At the commencement date, a lessee shall measure the right-of-use asset at cost.**

24 The cost of the right-of-use asset shall comprise:

- (a) the amount of the initial measurement of the lease liability, as described in paragraph 26;
- (b) any lease payments made at or before the commencement date, less any *lease incentives* received;
- (c) any *initial direct costs* incurred by the lessee; and
- (d) an estimate of costs to be incurred by the lessee in dismantling and removing the underlying asset, restoring the site on which it is located or restoring the underlying asset to the condition required by the terms and conditions of the lease, unless those costs are incurred to produce inventories. The lessee incurs the obligation for those costs either at the commencement date or as a consequence of having used the underlying asset during a particular period.”

**“26 At the commencement date, a lessee shall measure the lease liability at the present value of the lease payments that are not paid at that date. The lease payments shall be discounted using the *interest rate implicit in the lease*, if that rate can be readily determined. If that rate cannot be readily determined, the lessee shall use the *lessee’s incremental borrowing rate*.”**

**“Lease payments** Payments made by a lessee to a lessor relating to the right to use an underlying asset during the lease term, comprising the following:

- (a) **fixed payments** (including in-substance fixed payments), less any **lease incentives**;
- (b) **variable lease payments** that depend on an index or a rate;
- (c) the exercise price of a purchase option if the lessee is reasonably certain to exercise that option; and
- (d) payments of penalties for terminating the **lease**, if the lease term reflects the lessee exercising an option to terminate the lease

...”

From the above, the Committee notes that at the commencement date, the Company (as lessee) should recognise a right-of-use asset in respect of the underlying asset and a lease liability. At the commencement date, the Company should measure right-of-use asset at cost, which shall comprise the initial measurement of lease liability, *lease payments* made at or before the commencement date (less any lease incentives received), any initial direct costs incurred by the lessee and an estimate of costs to be incurred by the lessee in dismantling/removing and restoring the asset/site as per the terms and conditions of the lease (if any). The Company should also recognise a lease liability at the commencement date at the present value of the *lease payments* that are not paid at that date.

The Committee now examines the nature of GST in Indian context. The Committee notes that GST is a consumption based tax which is levied by the Government on the customer for consumption of services and therefore, is a statutory obligation towards the Government. Thus, the primary obligor for payment of GST is the customer who avails goods or services, though it is collected by the seller/vendor (who provides goods or services) on behalf of the Government. In case of leases, the lessor charges or collects GST on behalf of the tax authority and remits the same to the tax authorities (viz., acting only as collection agent for the government).

In this context, the Committee notes that the GST payments (irrespective of whether these are recoverable as input credit or not) do not meet the definition of lease payment (as reproduced above) as these are not payments to the lessor in exchange for the right to use of the underlying asset. Rather, as discussed above, GST payments are payments involving outflow of resources embodying economic benefits, imposed by the government on the lessee and are therefore, in the nature of *levies* as per paragraph 4 of Appendix C, ‘Levies’ of Ind AS 37, ‘Provisions, Contingent Liabilities and Contingent Assets’, reproduced as below:

“4. For the purposes of this Appendix, a levy is an outflow of resources embodying economic benefits that is imposed by governments on entities in accordance with legislation (ie laws and/or regulations), other than:

- (a) those outflows of resources that are within the scope of other Standards (such as income taxes that are within the scope of Ind AS 12, *Income Taxes*); and
- (b) fines or other penalties that are imposed for breaches of the legislation.

‘Government’ refers to government, government agencies and similar bodies whether local, national or international.”

Accordingly, the Committee is of the view that GST payments made by the Company as lessee in the extant case cannot be included in the measurement of the lease liability or right-of-use asset.

#### **D. Opinion**

17. On the basis of the above and subject to paragraph 15 above, the Committee is of the opinion that the GST payments made by the Company as lessee in the extant case cannot be included in the measurement of the lease liability or right-of-use asset, as discussed in paragraph 16 above.

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