

Commissioner of Income-tax, Gujarat-iv Vs. Saurashtra Cement and Chemical Industries Ltd.

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Court : Gujarat

Decided On : Aug-25-1975

Reported in : [1981]127ITR47(Guj)

Judge : B.J. Diwan, C.J. and; B.K. Mehta, J.

Acts : [Income Tax Act, 1961](#) - Sections 33

Appeal No. : Income-tax Reference No. 26 of 1973

Appellant : Commissioner of Income-tax, Gujarat-iv

Respondent : Saurashtra Cement and Chemical Industries Ltd.

Judgement :

Divan, C.J.

1. In this reference, at the instance of the revenue the following question has been referred to us by the Tribunal.

'Whether, on the facts and in the circumstances of the case, the Tribunal was right in law, in holding that Rs. 9,000 being the expenditure on cement factory lighting and Rs. 11,000 being the electrical expenses on that and trial runs for the cement plant, which had not started working should be considered as capital expenditure which should be added to the cost of construction of cement plant for purposes of depreciation and development rebate ?'

2. The assessee herein is a limited company and we are concerned with assessment year 1961-62. The assessee-company was started with the main object establishing and undertaking of manufacture of cement at Ranavav, near Porbandar, in Gujarat State. In the year of account relevant to the assessment year 1961-62, the assessee-company had not started cement production. The only business in the year of accounting was that of extraction of lime-stone, which is a raw material for manufacture of cement. In the year of account, the expenses for electric consumption had gone up from Rs. 3,032 for the immediately preceding year to Rs. 59,520 in the year of account relevant for the assessment year under consideration. The explanation given by the assessee was that electricity charges had gone up due to electrification of residential quarters, electrification of time office, stores and general officer, electrification of quarry office and colony street lights and due to tests and trials of the plant. The ITO allowed Rs. 4,000 out of the electricity expenses and disallowed the balance of Rs. 55,520 as relating to cement plant construction and of a capital nature. The assessee took the matter in appeal and the AAC held in appeal that Rs. 45,000 should be disallowed and should be treated as capital expenditure. The matter was taken in further appeal before the Tribunal by the assessee and the Tribunal held that 50 per cent. of the factory lighting and the whole of test and trial expenses for the plant could properly be related to the cement plant under construction, while other items like colony lighting, office lighting, etc., should be treated as expenditure in connection with the lime-stone business which was carried on by the assessee and that these expenses would have been incurred, whether

the new plant was undertaken or not. The Tribunal held that Rs. 9,000 out of factory lighting and Rs. 11,000 for test and trial runs should be disallowed and should be treated as capital expenditure. The Tribunal also directed that this allowance should qualify for depreciation and development rebate being capital expenditure toward cost of erecting cement plant and should be added to such expenditure.

3. The main grievance of the revenue before us is that the Tribunal has allowed the amount of Rs. 11,900 particularly being expenses for the consumption of electricity for test and trial as capital expenditure. It is clear that so far as the sum of Rs. 9,000 was concerned, that was the amount which was spent by the assessee-company for factory lighting and since the factory had not yet gone into actual production, these would be preliminary expenses.

4. We find that the matter in controversy before us is concluded by the observations of the Supreme Court in *Challapalli Sugars Ltd. v. CIT* : [1975]98ITR167(SC) . Khanna J., delivering the judgment of the Supreme Court, has pointed out at page 172 :

'It has not been disputed that so far as the question before us is concerned the legal position for determining the actual cost for the purpose of development rebate is the same as for the purpose of depreciation.

It would appear... that, while considering the question of deduction on account of depreciation and development rebate, we have to take into account the written down value. Written down value in its turn depends upon the actual cost of the assets to the assessee. The expression 'actual cost' has not been defined in the Act, and the question which engages our attention is whether the interest paid before the commencement of production on the amount borrowed for the acquisition and installation of the plant and machinery can be considered to be part of the actual cost of the assets to the assessee.'

5. After considering several provisions of the Companies Act and what has been observed in *Accountancy by Pickles, and Spicer & Pegler's Practical Auditing*, Khanna J., observed at page 175 :

'It would appear from the above that the accepted accountancy rule for determining the cost of fixed assets is to include all expenditure necessary to bring such assets into existence and to put them in working condition.'

6. The Supreme Court accepted this accountancy rule for the purpose of determining the actual cost of assets to the assessee. The expenses required for bringing the assets into working condition are considered by accepted accountancy rule as part of the cost of assets and this being the observation of the Supreme Court regarding the accepted accountancy rule, it is obvious that in the case before us, the amount of Rs. 11,900 which was required for test and trial was necessary for putting the plant in working condition. It is commonsense and matter knowledge that the test and trial of the plant has in the plant and machinery can be detected at an early stage and can be rectified, and, without test and trial no plant can ever go into actual regular production. Under these circumstances, the amount of Rs. 11,900 incurred for test and trial can properly be considered as part of the cost of fixed assets to the assessee and hence can be taken into consideration as part of the capital expenditure which would qualify for depreciation and development rebate.

7. In view of the above discussion, we hold that the Tribunal was right in law in holding that Rs. 9,000 being the expenditure on cement factory lighting and Rs. 11,000 being electrical expenses on test and trial runs for the cement plant, which had not started working, should be considered as capital expenditure. It should be added to the cost of construction of cement plant for purposes of depreciation and development rebate. We, therefore, answer the question referred to us in the affirmative and against the revenue. In view of the fact that prior to the decision of the Supreme Court, the legal position was not settled, there will be no order as to costs of this reference.