

+ ITA 160/2012

CIT

..... Appellant
Through Mr. Sanjeev Sabharwal, Sr. Standing
Counsel.

versus

IMPERIAL FASTNERS P LTD

..... Respondent
Through Mr. Sandeep Sapra, Advocate.

CORAM:**HON'BLE MR. JUSTICE SANJIV KHANNA****HON'BLE MR. JUSTICE R.V.EASWAR****ORDER**% **25.04.2012**

Revenue in this appeal under Section 260A of the Income Tax Act, 1961 (Act) impugns the order dated 17th June, 2011 passed by the Income Tax Appellate Tribunal (tribunal) in the case of Imperial Fasteners Pvt. Ltd., the respondent-assessee. The appeal pertains to the assessment year 2006-07.

2. Having heard learned counsel for the parties, we frame the following substantial question of law:-

“Whether the Income Tax Appellate Tribunal was right in holding that the expenditure of Rs.31,54,844/- was a revenue expenditure and not a capital expenditure?”

3. As we have heard learned counsel for the parties, we proceed to

dictate our decision.

4. The respondent-assessee is a company and for the assessment year in question it had filed its return of income on 8th December, 2006 declaring loss of Rs.19,84,799/- under the normal provisions and book profit of Rs.7,36,458/- under Section 115JB of the Act. The Assessing Officer in the assessment order has recorded that the assessee had debited a sum of Rs.31,54,844/- in the computation of income as deferred revenue expense and 10% of the said amount was debited to the profit and loss account as deferred revenue expenditure. The assessee was accordingly asked to justify why for the taxation purpose the assessee had treated the entire amount as revenue expenditure. The assessee gave their explanation, which was not accepted by the Assessing Officer, who held that the expenditure incurred had given enduring benefit to the assessee for a period of 10 years i.e. the period of lease. Accordingly, the Assessing Officer disallowed the claim by treating the entire expense as incurred on capital account. Even depreciation was not allowed.

5. The CIT (Appeals) affirmed the aforesaid findings given by the Assessing Officer.

6. In the second appeal before the tribunal, it has been held that the expenditure incurred was a revenue expense and should be allowed.

7. It is an undisputed fact that the respondent-assessee had entered into an agreement with the Central Coalfield Limited, Ranchi for taking on lease their thermal power station at Kathara. As per the lease deed, the respondent-assessee was to pay monthly lease rent and the ownership continued to remain with the Central Coalfield Limited. The respondent-assessee was to operate and maintain power station in addition to carrying out other works. The lease could be terminated in certain circumstances.

8. The tribunal has referred to the expenditure in question, which is as under:-

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Sr	Supplier	Date	Bill No.	Description of Goods	Nature of Expenditure	Amount (Rs.)
1.	Vinsoil Oil Company, J-2/6B, Rajouri Garden, New Delhi-110027	06.08.05	001	T.R. Oil	For Lubrication of parts of plant for its running	443,906
2.	Balaji Industrial Products Ltd., 117 & 119, Industrial Area, Jothwara, Jaipur-302012	23.09.05	014	Steel Hammer (Coal Crusher)	Replacement	227,908
3.	Savita Chemicals Ltd., Plot No.10/2, Kharapada, P.O. Naroli, Silvasa 396230	17.10.05	4722	Turbine Fluid	For movement of Turbine	633,764
4.	Exsol Energy Systems, The Cranium, 24, Top	13.12.05	345	Lead Acid Stationery Cell	Replacement	530,000

	Floor, Adhchini, New Delhi- 110017			Batteries		
5.	Eagle Poonawala Industries, 212/2, Hadapsar, Off s\Soil Poonawal Road, Pune- 411028	10.03.06	8408	Mechanical Parts	Replacement	143,899 .60
6.	Advant Automation Solutions Private Limited, 11/124, Indira Nagar, Lucknow (U.P)	13.3.06	0139	Hot Well Level Switch Hot Well	Replacement	107,640
7.	R.K. Automobiles (P) Ltd. 2620/3, Hamilton Road, Kashmere Gate, Delhi-6.	16.03.06	1245	Valves Bearings Oil Seals etc.	Replacement	208,000
8.	Anil Rubber Mills (P) Ltd. Plot no.30, Sector-6, Faridabad 121006	25.03.06	146	Conveyor Belt	Replacement	750,031
9.	Dhanbad Electro Power Meters, 28, Binod Market, (Near Court More), Hirapur, Dhanbad 860002	31.01.06	06	Electric Meter	Replacement	109,695
TOTAL						3,154,843.60

9. We may note that the two expenses i.e. expense of Rs.4,43,906/- on T.R. Oil meant for lubrication of the equipment and Rs.2,27,908/- on replacement of Steel Hammer (Coal Crusher) were incurred before the lease agreement dated 14th October, 2005 was executed between the respondent-assessee and the Central Coalfield Limited.

10. The tribunal after referring to the nature and character of the expenses, which have been incurred and after examining the terms of the lease, came to the conclusion that the lease in question required the assessee to incur expenses relating to current repair and maintenance to make the plant operational and start running. It has been recorded by the tribunal that replacement and other parts, purchased and installed by the assessee were relating to normal wear and tear and the same did not have a long life. The findings recorded by the tribunal, in this regard are:-

“8. Right from the beginning it has been the claim of the assessee that the nature of expenditure incurred by the assessee is revenue. From the details it can be seen that none of the expenditure has created any item of capital asset. It is in the nature of lubricating oil, replace of steel hammer, turbine fluid for movement of turbine, lead acid stationery cell batteries which have been replaced, mechanical parts which have been replaced and other items of replacement like hot well level, valves bearings oil seals, conveyor belt and electrical meter. If assessee has to bring the plant in working order and to run it, these expenditure are necessary in regular course and they represents day to day expenditure either in the nature of current repair or in respect of wear and tear of the plant and machinery. Therefore, none of these expenditures have created any capital asset to the assessee and they are not in the nature of capital expenditure.”

11. Thereafter, the tribunal has referred to the clauses of the lease agreement which stipulated that the lease was for a period of 20 years

from 14th October, 2005 and would be subject to payment of monthly rent of Rs.32,00,000/-, which was to start from 14th April, 2006. Under clause 4.1, the scope of work/obligation assigned to the assessee included maintenance of the plant and equipments and carry out inspection, overhauling and repair of boilers. Reference is also made to clause 17.3, which relates to surrender on termination of the lease. The said clause reads :-

“17.3 At the expiration or sooner determination of demise, the lessee shall yield up and deliver upon lesser peaceful possession of the station in good running condition without claiming any compensation value thereof but lesser shall pay to the lessee written down value of the additions and alterations of the building, station or additional machinery that may be brought by the lessee at the station. On such determination the schedule station shall rest in and be the absolute property of lesser.”

12. Another clause in the lease stipulated that it was the obligation of the respondent-assessee to supply electricity to the lessor at a prescribed rate. After examining the clauses the tribunal has held:-

“10. A cumulative reading of all these clauses will show that assessee was to operate the plant of generation of electricity and part of the generation of electricity was to be supplied to the lessor at prescribed rates. The assessee was to incur expenses on repairs and maintenance of the plant was to generate electricity and generate revenue in the year under consideration but the payment of lease rent was to start from 14th April, 2006 which date falls in the next financial year. The term of lease is 20 years. As per clause 17.3, upon expiration of lease, the

assessee was to handover the plant in good running condition except liability of lessor to pay to the assessee the written down value of the additions and alterations of the building, station or additional machinery that may be brought by the lessor at the station and on such determination the schedule station shall rest in and be the absolute property of the lesser. Thus, this clause conveys that what the assessee is entitled is only written down value of the additions and alterations to the building, station or additional machinery. The aforesaid detail will reveal that none of the items represents addition or alteration to the building, station or additional machinery. Therefore, the amount of expenditure incurred by the assessee cannot be said to be giving any enduring benefit to the assessee. It has not created any capital asset for the assessee. Therefore, keeping in view the terms of agreement and facts of the case, it cannot be said that the expenditure incurred by the assessee has given any enduring benefit.”

13. Looking at nature of the expenses, which have been incurred by the respondent-assessee and the conditions stipulated and mentioned in the lease agreement, the tribunal has rightly held that the aforesaid expenses were in nature of current repair either for making the plant/factory operational or to replace the damaged or unserviceable parts to run/start the plant.

14. The Assessing Officer in the assessment order had not dealt with the nature and specifications of repair undertaken or the purchases made. Further to classify an expenditure as current repairs or capital, the foremost requirement is to see whether repair

undertaken is to preserve and maintain or operationalize/operate the already existing asset or bring into existence a new asset. Also, the amount/quantum of money alone cannot be factor to determine whether the expenditure falls under current repair or revenue expenditure. The Supreme Court in ***Commissioner of Income Tax v. Saravana Spg. Mills (P) Ltd.***, (2007) 7 SCC 298, has held :

“5. This Court in *Ballimal Naval Kishore v. CIT* approved the test formulated by Chagla, C.J. in *New Shorrock Spg. and Mfg. Co. Ltd. v. CIT* as to when the expenditure can be said to have been incurred on current repairs. In that case it was observed as follows: (*New Shorrock case*, ITR pp. 343-44)

“The simple test that must be constantly borne in mind is that as a result of the expenditure which is claimed as an expenditure for repairs what is really being done is to preserve and maintain an already existing asset. The object of the expenditure is not to bring a new asset into existence, nor is its object the obtaining of a new or fresh advantage. This can be the only definition of ‘repairs’ because it is only by reason of this definition of repairs that the expenditure is a revenue expenditure.

If the amount spent was for the purpose of bringing into existence a new asset or obtaining a new advantage, then obviously such an expenditure would not be an expenditure of a revenue nature but it would be a capital expenditure, and it is clear that the deduction which the legislature has permitted under Section 10(2)(v) is a deduction where the expenditure is a revenue expenditure and not a capital expenditure.”

In the said judgment, it has been further observed by Chagla, C.J. that the definition of the word “repair” does not create much difficulty, but the difficulty is

created by the word “current” which qualifies the expression “repair”. This adjective, namely, “current” is put in by the legislature. It indicates that the legislature did not intend that the assessee should be permitted to claim allowance for all kinds of repairs, *even though conceptually the expenditure may be revenue expenditure*. The legislature intended to stress that under Section 31(i) the permissible deduction admissible is only for current repairs, therefore, the question as to whether the expenditure incurred by the assessee conceptually is revenue or capital in nature is not relevant for deciding the question as to whether such an expenditure comes within the etymological meaning of the expression “current repairs”. In other words, even if the expenditure is revenue, it may not fall in the connotation of “current repairs” in Section 31(i). The test formulated above applies to cases where the assessee claims allowance under Section 31(i).

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11. An allowance is granted by Clause (i) of Section 31 in respect of amount expended on current repairs to machinery, plant or furniture used for the purposes of business, irrespective of whether the assessee is the owner of the assets or has only used them. The expression “current repairs” denotes repairs which are attended to when the need for them arises from the viewpoint of a businessman. The word “repair” involves renewal. However, the words used in Section 31(i) are “current repairs”. The object behind Section 31(i) is to preserve and maintain the asset and not to bring in a new asset. In our view, Section 31(i) limits the scope of allowability of expenditure as deduction in respect of repairs made to machinery, plant or furniture by restricting it to the concept of “current repairs”. All repairs are not current repairs. Section 37(1) allows claims for expenditure which are not of capital nature. However, even Section 37(1) excludes those items of expenditure which expressly falls in Sections 30 to 36. The effect is to delimit the scope of allowability of deductions for repairs to the extent provided for in Sections 30 to 36.

12. To decide the applicability of Section 31(i) the test is not whether the expenditure is revenue or capital in nature, which test has been wrongly applied by the High Court, but whether the expenditure is “current repairs”. The basic test to find out as to what would constitute current repairs is that the expenditure must have been incurred to “preserve and maintain” an already existing asset, and the object of the expenditure must not be to bring a new asset into existence or to obtain a new advantage.”

14. Counsel for the Revenue has not been able to point out and show that the aforesaid expenses were not incurred on replacement of parts, lubrication etc. No new asset came into existence. The expenditure was incurred to make the plant operational and functional. We may note that in the assessment year in question the plant in fact became operational and 22,53,500 units of power were generated and sold for Rs.61,17,125/- as per the audited accounts.

15. The question of law accordingly is answered in affirmative i.e. in favour of the respondent-assessee and against the Revenue. The appeal is dismissed without any order as to costs.

SANJIV KHANNA, J.

R.V.EASWAR, J.

APRIL 25, 2012

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