(2004) 08 AHC CK 0141

In the Allahabad High Court

Case No : IT Ref. No. 192 of 1983

Commissioner of Income Tax — APPELLANT

Vs

Mohan Steel Ltd. — RESPONDENT

Date of Decision : 31-08-2004

Acts Referred:
Income Tax Act, 1961 — Section 37, 37(1)

Citation : (2004) 191 CTR 279 : (2005) 273 ITR 479

Hon'ble Judges : R.K. Agrawal, J;K.N. Ojha, J

Bench : Division Bench

Advocate : A.N. Mahajan, for the Appellant; None, for the Respondent

Judgement

R.K. Agrawal, J.—The Tribunal, Allahabad; has referred the following question of law u/s 256(1) of the IT Act, 1961 (hereinafter referred to as "the Act"), for opinion to this Court :

"Whether, on the facts and in the circumstances of the case, the Tribunal was justified in law in holding that the expenditure incurred by the assessee before the commencement of the actual production was allowable as a revenue expenditure and not as a capital expenditure ?"

2. Briefly stated, the facts giving rise to the present reference are as follows :

The reference relates to the asst. yr. 1977-78. The relevant previous year ended on 31st March, 1977. For the assessment year in question, the respondent filed its return of income declaring a loss of Rs. 9,86,734. As it had not commenced any manufacturing activity, the IAC (Asst.) called upon the respondent to show cause as to why various expenses debited in the P&L a/c should not be disallowed and its income should be assessed at nil. The respondent submitted that it had set up its steel plant on 15th Feb., 1975, but could not commence the production due to non-availability of supply of electricity by the State Government and as soon as the electricity was supplied on 4th Nov., 1978, it had started its manufacturing activity within 45 minutes of the supply thereof. It also pointed out that in the immediately preceding two years, the AO had framed the assessment u/s 143(3) of the Act and had treated the expenses claimed by it as revenue expenditure and computed the loss which was allowed to be carried forward. It was submitted that once the Revenue had already accepted that it had commenced its business a couple of years back, it would not be fair and reasonable to hold that the expenses claimed by it for the assessment year in question should not be allowed and instead of loss shown by it the income should not be (sic-should be) assessed at nil. The AO did not agree with the contention of the respondent and assessed the income at nil. In appeal, the CIT(A) held that the items of expenditure shown by the respondent are revenue expenditure and are allowable. However, he remanded the matter for recomputation of loss. The Tribunal has upheld the order passed by the CIT(A).

3. We have heard Sri A.N. Mahajan, the learned counsel for the Revenue. Nobody has appeared on behalf of the respondent.

4. Sri Mahajan, learned counsel, submitted that admittedly the respondent had not commenced its production during the previous year relevant to the assessment year in question as it had commenced the production only on 4th Nov., 1978, which fell in the asst. yr. 1979-80 and, therefore, in the absence of any business, the expenses could not be claimed as a deduction. He referred to the express provision of Section 37 of the Act.

5. It is not in dispute that the respondent had commenced production only on 4th Nov., 1978. Section 37 of the Act under which the expenditure incurred wholly and exclusively for the purposes of business, is allowed as deduction, presupposes that the business had commenced or is being carried on.

6. The Bombay High Court in the case of Commissioner of Income Tax, Bombay City-II Vs. Industrial Solvents and Chemicals Pvt. Ltd., , Commissioner of Income Tax, Bombay City-III Vs. Forging and Stamping Pvt. Ltd., and J.R. Mehta Vs. Commissioner of Income Tax, Bombay City-II, has held that if during the relevant period there was no business, the question of allowability of expenses would not arise. Similar view has been taken by the Andhra Pradesh High Court in the case of Commissioner of Income Tax Vs. Omer Khayyam Wineries (P.) Ltd., and the Kerala High Court in the case of S.P.V. Bank Ltd. Vs. Commissioner of Income Tax, and T.M. Chacko and Partners Vs. Commissioner of Income Tax,

7. The apex Court in the case of The Eimco K.C.P., Madras Vs. Commissioner of Income Tax, Madras, while considering the scope of Section 37 of the Act has held as follows :

"A plain reading of the above provision makes it clear that it is a residuary provision and allows an expenditure not covered under Sections 30 to 36 in computing the income chargeable under the head ''Profits and gains of business or profession'', on fulfilment of the other requirements, namely (i) the expenditure should not be in the nature of capital expenditure or personal expenses of the assessee; (ii) it should have been laid out or expended wholly and exclusively for the purposes of the business or profession; (iii) it should have been expended in previous year."

It has held as follows :

"What in effect was done by the appellant in allotting equity shares of Rs. 2,80,000 to Eimco, was to reimburse the contribution of Eimco by way of know-how, which can never be treated as expenditure, much less an expenditure laid out wholly and exclusively for purposes of the business of the appellant. It is not a case where after the incorporation, the appellant-company in the course of carrying on its business, spent the said amount for acquiring any asset."

The aforesaid decision has subsequently been followed by the apex Court (sic-Delhi High Court) in the case of CIT v. Reinz Talbros (P) Ltd. (2001) 262 ITR 637.

8. We are in respectful agreement with the view taken in the aforesaid cases.

Respectfully following the principle laid down by the apex Court, we are of the considered opinion that the expenses incurred by the respondent before the commencement of the business, cannot be considered as a revenue expenditure u/s 37 of the Act. We, therefore, answer the question, referred to us, in the negative, i.e., in favour of the Revenue and against the assessee. There shall be no order as to costs.