


# ***IT 2618 - Income tax: depreciation - cost of erecting plant - expenditure on construction camps for use by contractor's employees***

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TAXATION RULING NO. IT 2618

INCOME TAX: DEPRECIATION COST OF ERECTING PLANT -  
EXPENDITURE ON CONSTRUCTION CAMPS FOR USE  
BY CONTRACTOR'S EMPLOYEES

FOI Embargo: May be released

REF

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I 1012412	DEPRECIATION COST OF PLANT CONSTRUCTION CAMP	54 56(1)

OTHER RULINGS ON THIS TOPIC: IT 21, IT 2181, IT 2197

PREAMBLE

A deduction is allowable under the income tax law for depreciation on a unit of property, being plant or articles, owned by a taxpayer and used to produce assessable income. The deduction is calculated as a percentage of the cost or written down value (i.e., the initial cost less depreciation previously allowed or allowable) of the unit of property.

2. This Ruling is concerned with the meaning of the term "cost" in paragraph 56(1)(b) of the Income Tax Assessment Act 1936 ("the Act") in relation to a unit of property and the application of that term in a particular situation considered by this Office.

3. Before proceeding, however, it is desirable to draw attention to the distinction made in paragraphs 3 and 4 of Taxation Ruling IT 2197 between two categories of expenditure associated with the installation of plant and equipment, namely installation expenses and costs of structural alterations and ancillary items of plant.

4. As stated in IT 2197, installation expenses embrace such items as freight and delivery costs, customs duty and other import levies, minor rearrangements and removal of plant and equipment within relevant premises - i.e., expenses which may be incurred in getting the plant and equipment to the site and putting it in place. On the other hand, structural alterations and ancillary items of plant and equipment cover expenses which may be necessary to make way for the new plant and equipment, e.g., the demolition of existing plant and equipment and consequent clearing of a site, structural alterations to a building etc. It also covers ancillary items of equipment which may be necessary to the operation of the major items of new plant and equipment, e.g., a free access floor for a computer.

5. The situation considered in this Ruling does not involve the

installation of an item of movable plant or equipment. Rather, like the construction of the oil refinery involved in B.P. Refinery (Kwinana) Ltd v. FCT (1961) ALR 52; (1960) 12 ATD 204, it involves a project for the construction by a cement manufacturer of a slurry production plant and an associated clinker production plant. As part of that project, construction camps were erected by the taxpayer to house employees of the contractor engaged to construct these plants.

#### FACTS

6. The project for the construction of the slurry and clinker production plants involved the taxpayer in many contracts entered into for the supply of components and other items of plant. Each contract required the taxpayer, at its expense and not at the contractor's expense, to provide camp accommodation and mess facilities for the employees because of the remoteness of the construction sites.

7. The camp and associated facilities were of a temporary nature and on completion of the construction work were all sold or scrapped.

8. Included in the cost of establishing the construction camps was expenditure by the taxpayer on the following:

- . demountable huts
- . concrete pathways
- . carparks
- . surfacing of access roads
- . electricity lines and poles
- . sewerage treatment plant and connections
- . kitchen equipment
- . washing machines
- . curtains
- . desks, chairs, tables, beds, pillows and linen
- . playground equipment
- . television sets
- . movie projectors
- . dartboards
- . billiard tables.

#### RULING

9. The costs involved in establishing the construction camps and their associated facilities constituted part of the cost of the slurry and clinker production plants for the purpose of calculating the depreciation allowable on such parts of these plants as were "plant or articles" in terms of section 54 of the Act.

10. The expenditure on the camps here was similar to that involved in the B.P. Refinery (Kwinana) case. There, the taxpayer entered into a contract for the construction of an oil refinery. The contract price consisted of a fixed fee plus an amount equal to all expenditure incurred by the contractor in carrying out the work. In the course of constructing the refinery, the contractor erected a number of temporary buildings, including a camp for the accommodation of workmen, temporary

offices, tool rooms and sheds. When the construction had been completed, most of the temporary buildings were demolished and the remainder handed over to the taxpayer. All the buildings were used solely for purposes incidental to the construction of the refinery. The net cost of the temporary buildings (after deducting proceeds of sale of materials salvaged and the residual value of buildings handed over) was 185,001 Pounds and this amount was paid by the taxpayer to the contractor as part of the contract price. Of that amount, 172,661 Pounds related to units of property which were in the nature of plant. The taxpayer claimed, but the Commissioner disallowed, an amount of 6,104 Pounds for depreciation in respect of these units.

11. The High Court of Australia (Kitto J.) held that the method adopted by the taxpayer in apportioning the indirect cost of the temporary buildings was appropriate in that case and that the amount so apportioned to plant formed part of the cost of the refinery for purposes of paragraph 56(1)(b) of the Act and depreciation was allowed accordingly.

12. The B.P. Refinery (Kwinana) case is not materially different from the present case. The cost of the construction camp and its associated facilities provided for the contractor's employees were therefore apportioned over the cost of the slurry and clinker production plants.

13. The expenditure in the B.P. Refinery (Kwinana) case was incurred, at least initially, by the contractor in the course of constructing the refinery. Here, however, the expenditure on the camps was incurred by the taxpayer directly and not by the contractor. Moreover, the expenditure by the taxpayer in the B.P. Refinery (Kwinana) case formed part of the contract price whereas the expenditure by the taxpayer, in a sense, brought into existence specific business assets over which the taxpayer had total control. While these assets were used only for the purpose of housing the contractor's employees while the plants were being constructed, the taxpayer had the right to retain or dispose of them once the plants were constructed.

14. Notwithstanding these factual differences, however, the essential question remains whether the expenditure incurred by the taxpayer on the camps and their associated facilities forms part of the cost of the plants that were constructed.

15. It was essential to the construction of the slurry and clinker production plants that the temporary camps and the facilities be provided. The expenditure was incurred in the course of constructing the plants and is therefore analogous to the installation expenses referred to in IT 2197 (paragraph 3) which were incurred in getting the plant and equipment to the site and putting it in place. The close connection between the cost of the camps and the cost of the plants is also further evidenced by the disposal of the camps on the completion of the construction. In the circumstances, it is reasonable to accept that the cost of the camps formed part of the total cost to the taxpayer of the finished slurry and clinker production plants.

16. For these reasons, the expenditure incurred by the taxpayer on the construction camps and their associated facilities were considered to be part of the cost of the plants and could be apportioned, on a reasonable basis, over the depreciable units of property. Proceeds received by the taxpayer from the sale of materials salvaged from the camps had to be subtracted from the total cost of the camps, as occurred in the B.P. Refinery (Kwinana) case, to arrive at the net cost of the camps.

17. Only expenditure on temporary buildings and facilities directly related to the construction of plant may be regarded as forming part of the cost of plant in situations similar to those outlined above. Any buildings or facilities of a permanent nature to be used as part of the taxpayer's business once construction of the plant is completed are considered to be capital assets separate and distinct from the plant. Their cost would not form part of the cost of the plant. Individually, however, some of these facilities may qualify for income tax deductions for depreciation in their own right provided the necessary tests are met.

COMMISSIONER OF TAXATION  
8 November 1990