

IN THE HIGH COURT OF UTTARAKHAND AT NAINITAL

Income Tax Appeal No. 19 of 2010

Commissioner of Income Tax. Appellant

Versus

Oil & Natural Gas Corporation Ltd. Respondent

Income Tax Appeal No. 20 of 2010

Commissioner of Income Tax. Appellant

Versus

Oil & Natural Gas Corporation Ltd. Respondent

Income Tax Appeal No. 21 of 2010

Commissioner of Income Tax. Appellant

Versus

Oil & Natural Gas Corporation Ltd. Respondent

&

Income Tax Appeal No. 22 of 2010

Commissioner of Income Tax. Appellant

Versus

Oil & Natural Gas Corporation Ltd. Respondent

Mr. H.M. Bhatia, Advocate for the appellant.
Mr. Rupesh Jain, Advocate for the respondent.

JUDGMENT

**Coram: Hon'ble K.M. Joseph, C.J.
Hon'ble V.K. Bist, J.**

Dated: 14th May, 2015

K.M. JOSEPH, C.J. (Oral)

These matters being interconnected, they are being disposed of by this common judgment.

2. The only substantial question of law, which is raised in these appeals, is whether the ITAT has erred in law in holding that the expenditure incurred on Dry Docking Expenses are revenue in nature.

3. Incidentally, Income Tax Appeal Nos. 19 of 2010 and 22 of 2010 relate to the very same assessment year, i.e. 2005-2006; but, according to the learned counsel for the appellant, the appeal and cross-appeal in the Tribunal occasioned the filing of the two appeals. We say this because the learned counsel for the respondent would point out that Income Tax Appeal No. 19 of 2010 may not be maintainable.

4. Respondent / assessee is engaged in oil exploration. The Assessing Officer disallowed the expenditure incurred by the respondent / assessee towards the maintenance of vessels and rigs on the basis that it will be a capital expenditure. In appeal, the appellate Commissioner allowed the appeal of the respondent / assessee holding that it is a revenue expenditure. This finding has been affirmed by the Tribunal. It is against the same that the Revenue has come up in appeals under Section 260-A of the Income Tax Act.

5. The relevant finding recorded by the Tribunal is being reproduced hereunder:

“15. We have considered the rival submissions and perused the material on record and have gone through the orders of authorities below. We find that the AO has disallowed this claim in the present year on the basis that in Asstt. Year 2001-02, learned CIT(A) has decided this issue against the assessee. In Asstt. Year 2001-02, the assessee has explained the expenses on the basis that these are in the nature of repairs and maintenance and to fulfil the requirements of American Bureau Standards (ABS), for which, various surveys are to be undertaken, some of which are to be taken yearly, some are to be undertaken two and half yearly and

remaining are to be undertaken five yearly. It has been pointed out that it is obligatory on the part of ONGC to carry out surveys as per ABS for insurance and other purposes like requirement of mandatory authorities and hence, these expenses are revenue expenditure in the nature of repairs and maintenance but still in that year, the issue was decided by the AO against the assessee by stating that the claim of the assessee is devoid of merits as aforesaid expenses are clearly capital expenditure. No reasoning is given in the assessment order as to how these expenses are of capital nature. CIT(A) in that year has noted in para 9 of his order that the assessee in its written submissions has explained the nature of Dry Docking expenses and it is apparent from the description that the expenditure involved are not just repair but total overhaul and renovation of the vessels. He further stated that assessee had also not been claiming these expenses as revenue expenditure in its books of accounts and these expenses are not debited to profit and loss account as discussed in assessment order and by making these observations, learned CIT(A) in that year has upheld the assessment order. When we go through these explanations of the assessee as reproduced by the AO in the assessment order for that year and also the explanations given by the assessee before us, we are satisfied that these expenses are to keep the vessels in working condition and to fulfil the mandatory requirements of various authorities and for safety purpose and it does not enhance or improve the capacity of the vessels and hence, these expenses cannot be classified as capital expenditure. We, therefore, decide this issue in principle in favour of the assessee and hold that Dry Docking expenses are revenue in nature but for the qualification of the amount, we find that the details are not before us. The AO in the assessment order for Asstt. Year 2004-05 says that the assessee has incurred an expenditure of Rs. 111.62 crores and claimed the same as deduction on account of Dry Docking expenses in the computation of income but this is not clear as to whether this amount of Rs. 111.62 crores is the total amount of such expenses or whether a part of the total amount has already been debited in the P&L account on the basis of amortization of expenditure and this amount of Rs. 111.62 crores is remaining part of the total expenditure. This is also not clear as to whether the expenses debited in the present year to the P&L account with regard to earlier years has been added back in the computation of the assessee or not, as submitted by assessee before the AO because the AO has started the computation with the figures of income declared by the assessee as present year income and assessee has not furnished before us computation of income filed by it along with return of income and the profit and loss account for the relevant years. Under these facts, we feel that for the purpose of verification of the amount actually incurred by the assessee on this account in these three years, the matter should go back to the file of AO. We, therefore, restore this matter back to the file of AO in all the three years for the limited purpose of verifying the amount of deduction claimed by the assessee and the amount of actual expenditure incurred by the assessee in the relevant years.

Deduction should be allowed by the AO to the extent of the amount incurred by the assessee for this purpose in the relevant year ensuring that any amount debited in the profit and loss account for the relevant years on account of such expenses of earlier years should be added back in the computation of income if the same were not already added back by the assessee in its computation. With these observations, this issue in all the three years is restored back to the file of AO for this limited purpose. The AO should pass necessary orders as per law as per above discussion in all the three years after providing adequate opportunity of being heard to the assessee.”

6. Mr. H.M. Bhatia, learned counsel appearing for the appellant, would submit, essentially, that this is a case, where the respondent / assessee, in his own accounts, has not laid the foundation by debiting the profit and loss account by the amount allegedly spent towards maintenance of the rig and it was claimed to be capital expenditure and, in fact, the Assessing Officer was pleased to accept the claim and even provided depreciation at the rate of 25 per cent and only the balance amount has been disallowed being treated as capital expenditure.

7. Per contra, the learned counsel for the respondent / assessee would submit that there is an alternate claim of depreciation and the main claim was that it is a revenue expenditure; but, he does admit that, in the accounts, the amount claimed as spent towards maintenance was not debited to the profit and loss account; but his contention is that the accountancy practice cannot be treated as conclusive. In this context, he drew our attention to the unreported judgment of the Hon’ble Apex Court in Civil Appeal Nos. 6366-6368 of 2003 with Civil Appeal Nos. 6946-6948 of 2004 dated 23rd March, 2015. Therein, we notice the following finding:

“19. In the instant case, as noticed above, the assessee did not want spread over of this expenditure over a period of five years as in the return filed by it, it had claimed the entire interest paid upfront as deductible expenditure in the same year. In such a situation, when this course of action was permissible in law to the assessee as it was in consonance with the provisions of the Act which permit the assessee to claim the expenditure in the year in which it was incurred, merely because a different treatment was

given in the books of accounts cannot be a factor which would deprive the assessee from claiming the entire expenditure as a deduction. It has been held repeatedly by this Court that entries in the books of accounts are not determinative or conclusive and the matter is to be examined on the touchstone of provisions contained in the Act. [See – **Kedarnath Jute Manufacturing Co. Ltd. v. Commissioner of Income Tax (Central), Calcutta (1972) 3 SCC 252; Tuticorin Alkali Chemicals & Fertilizers Ltd, Madras v. Commissioner of Income Tax, Madras (1997) 6 SCC 117; Sutlej Cotton Mills Ltd. v. Commissioner of Income Tax, Calcutta (1978) 4 SCC 358; and United Commercial Bank, Calcutta v. Commissioner of Income Tax, WB-III, Calcutta (1999) 8 SCC 338.]”**

8. There are well known tests for determining whether expenditure fulfills the requirement of Section 37 of the Act and would amount to revenue expenditure or capital expenditure. In fact, the Assessing Officer proceeded on the basis that the Dry Docking expenses were held to be capital expenditure in nature by the Commissioner of Income Tax in deciding the assessment for the year 2001-2002 and the same are treated as capital expenditure. Though a large body of case-law was cited, the Assessing Officer proceeded to hold that the cases are quite distinguishable from the facts of the assessee’s case under consideration, inasmuch as, none of the cases related to the issue of shifting or floating vessel, which was involved in these cases. The appellate Tribunal, finding that it was not in a position to arrive at the exact amount, which could be claimed as the revenue expenditure, has remitted the matter back. We also notice the following finding by the Commissioner of Income Tax (Appeals):

“8.2 I have gone through the order of the AO and the submissions of the AR very carefully. Under the Merchant Shipping Act, every floating rigs and vessels have to undergo a compulsory survey within specified intervals in order to determine whether it is seaworthy and can withstand the safety standards laid out. Under such surveys, the structural and mechanical fitness of a floating installation is tested. The expenses on dry docking are on account of removing the old paint and repainting the same, overhauling the propellers, thrusters, gears and electric motors, repair and replacement / upgrading of the obsolete equipments. Such expenses are, therefore, only for maintaining and preserving the existing assets. The Allahabad High Court in the case of CIT Vs. B. Hill & Co. Pvt. Ltd. 142 ITR 188, following Supreme Court judgment in the case of CIT Vs. Kalyanji Mavji & Co. 122 ITR 49,

has held that expenditure for repair and reconstruction of already existing assets are revenue in nature. According to the accepted principles, capital expenditure is something which is spent once for all, while revenue expenditure is that which has to be incurred from year to year. If the expenditure is to bring into existence or advantage for the enduring profit of the business, then expenditure may be capital in the nature but where the expenditure has direct nexus, connection or relation to the carrying on or conducting the business of the assessee, it must be recorded as an integral part of profit making process and hence revenue in nature. The maintenance of these vessels and rigs is a sine-qua-non for carrying on its business of exploration and production of oil. In the case of the appellant, expenditure to the extent of Rs. 139,20,54,819/- was claimed as revenue. I am, therefore, of the opinion that AO was not right in disallowing the expenditure as capital expenditure. Appellant gets relief of Rs. 139,20,54,819/-. Appellant vide ground no. 4.2 has claimed that deptt. should allow depreciation on this expenditure considered as capital in A.Y. 2001-02 to 2003-04. AO is directed to allow depreciation on the WDV of capitalized value during this year.”

9. We are of the view that the view taken by the appellate authority, as affirmed by the Tribunal, cannot be faulted. In such circumstances, we are of the view that the question of law raised has to be answered against the Revenue. We do so and, consequently, the appeals fail and are dismissed. No order as to costs.

(V.K. Bist, J.)
14.05.2015

(K.M. Joseph, C. J.)
14.05.2015

G