

IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED: 23.01.2020

CORAM:

THE HON'BLE DR. JUSTICE VINEET KOTHARI
and
THE HON'BLE MR. JUSTICE R.SURESH KUMAR

Tax Case (Appeal)Nos.2117 to 2119 of 2008

M/s.Vedanta Limited
(Which is successor to Erstwhile Cairn India Limited)
[Appeal of Cairn Energy India Pty. Ltd.
Allowed to be continued by Erstwhile Cairn India Ltd.
Under Scheme of Arrangement approved
By Hon'ble Bombay High Court]
Core 6, 3rd Floor,
7, Lodhi Road,
New Delhi-110003
PAN:AACCS7101B
(Amended vide order dated 09.09.2019
made in C.M.P.Nos.13260, 13257 and
13256 of 2019 in TCA Nos.2117 to 2119 of 2008)

... Appellant
in all TCA's

...Vs..
सत्यमेव जयते

The Joint Commissioner of Income Tax,
Special Range-I,
No.121, Nungambakkam High Road,
Chennai-600 034.

... Respondent
in all TCA's

Prayers: Tax Cases (Appeals) are filed under Section 260-A of the Income

Tax Act, 1961, against the order of the Income Tax Appellate Tribunal, Chennai 'A' Bench, dated 24.07.2006 passed in I.T.A.Nos.490/MDS/2000, 352/MDS/2000 and 353/MDS/2002 for Assessment Year 1996-1997, 1997-1998 and 1998-1999.

For Appellant : Mr.R.V.Easwar
Sr.Advocate
M/s.Rubal Bansal
for Mr.P.Senthikumar

For Respondent : Mr.T.Ravikumar
Senior standing counsel

COMMON JUDGMENT

(Delivered by DR.VINEET KOTHARI, J.)

These Appeals have been filed by the Assessee raising the Substantial Questions of Law arising from the order of the learned Income Tax Appellate Tribunal dated 24.07.2006 for Assessment Years 1996-1997, 1997-1998 and 1998-1999.

2. These Appeals were admitted by the Co-ordinate Bench of this Court, on 28.01.2009 on the following Substantial Questions of Law:

T.C.(A)No.2117 of 2008

1. Whether on the facts and circumstances of the case, the Income Tax Appellate Tribunal was justified in law in holding that the amount of Rs.30,91,868/- debited in the profit and loss account towards provision for site restoration cost was not an allowable deduction under the Act.?"

T.C.(A)No.2118 of 2008

1. Whether on the facts and circumstances of the case, the Income Tax Appellate Tribunal was justified in law in holding that the amount of Rs.48,03,344/- debited in the profit and loss account towards provision for site restoration cost was not an allowable deduction under the Act.?"

T.C.(A)No.2119 of 2008

1. Whether in the absence of any specific ground of appeal, could it be held that, the Tribunal had impliedly held that, provision for site restoration cost is not an ascertained liability and, therefore adjustment could be made while computing the income under Section 115J of the Act?"

2. The learned Tribunal disallowed the provisions made by the Assessee for site restoration cost for the Assessment years in question by holding that "an expenditure which is deducted for income-tax purpose is one which is towards a liability actually existing at the time, but putting aside

some money which may become an expenditure on the happening of an event is not an expenditure." In other words, the Tribunal held that since the provision made under site restoration fund is a contingent liability incurred by the Assessee, the same is not an allowable expenditure. In paragraph 16 of the Impugned Order the Tribunal has clearly held that the provision for site restoration fund cannot be allowed even under Section 37 (1) of the Income Tax Act 1961 (in short 'Act') and therefore the Tribunal set aside the order of the Commissioner (Appeals) and restored the order of the Assessing Officer.

3. The Tribunal also referred to the provisions of Section 33ABA inserted by Finance Act (No.2) 1998 with effect from 01.04.1999 from which date such a provision for site restoration made by the Assessee cannot be allowed unless a actual deposit is made in the Site Restoration Fund under Section 33ABA of the Act. But the Assessment Years in question before us are prior to this amendment of law.

4.The three relevant provisions in this regard in the present case are Section 33ABA, Section 37 and Section 42 of the Income Tax Act 1961. Section 33ABA was inserted by Finance Act (No. 2) of 1998 with effect from 01.04.1999 is not applicable for three Assessment Years which are

Assessment Year 1996-1997 to 1998-1999. Further, the special provision for deductions in the case of business for prospecting, etc., for mineral oil for the purpose of computing the profits or gains of any business under Section 42 of the Act is also not presently relevant because the claim under Section 42 was given up by the learned Senior counsel for the Assessee Mr.R.V.Easwar appearing for the Assessee. Therefore the only question left for our consideration for deciding the controversy in hand is whether such deduction of 'Provision made for Site Restoration' by the Assessee can be allowed as a business expenditure under Section 37(1) of the Act.

5. The said three provisions of Act are quoted below for their relevant extent herein below:-

Section 33ABA

"33ABA.(1) *Where an assessee is carrying on business consisting of the prospecting for, or extraction or production of, petroleum or natural gas or both in India and in relation to which the Central Government has entered into an agreement with such assessee for such business, has before the end of the previous year—*

(a) deposited with the State Bank of India any amount or amounts in an account (hereafter in this section referred to as the special account) maintained by the assessee with that Bank in accordance with, and for the purposes specified in, a scheme (hereafter in this section referred to as the scheme) approved in this behalf by the Government of India in the Ministry of Petroleum and Natural Gas; or

(b) deposited any amount in an account (hereafter in this section referred to as the Site Restoration Account) opened by the assessee in accordance with, and for the purposes specified in, a scheme framed by the Ministry referred to in clause (a) (hereafter in this section referred to as the deposit scheme), the assessee shall, subject to the provisions of this section, be allowed a deduction (such deduction being allowed before the loss, if any, brought forward from earlier years is set off under [section 72](#)) of—

(i) a sum equal to the amount or the aggregate of the amounts so deposited; or

(ii) a sum equal to twenty per cent of the profits of such business (computed under the head "Profits and gains of business or profession" before making any deduction under this section),

whichever is less :

Provided that where such assessee is a firm, or any association of persons or any body of individuals, the deduction under this section shall not be allowed in the computation of the income of any partner or, as the case may be, any member of such firm, association of persons or body of individuals :

Provided further that where any deduction, in respect of any amount deposited in the special account, or in the Site Restoration Account, has been allowed under this sub-section in any previous year, no deduction shall be allowed in respect of such amount in any other previous year :

Provided also that any amount credited in the special account or the Site Restoration Account by way of interest shall be deemed to be a deposit.

(2) The deduction under sub-section (1) shall not be admissible unless the accounts of such business of the assessee for the previous year relevant to the assessment year for which the deduction is claimed have been audited by an accountant as defined in the Explanation below sub-section (2) of **section 288** and the assessee furnishes, along with his return of income, the report of such audit in the prescribed form duly signed and verified by such accountant :

Provided that in a case where the assessee is required by or under any other law to get his accounts audited, it shall be sufficient compliance with the provisions of this sub-section if such assessee gets the accounts of such business audited under such law and furnishes the report of the audit as required under such other law and a further report in the form prescribed under this sub-section.

(3) Any amount standing to the credit of the assessee in the special account or the Site Restoration Account shall not be allowed to be withdrawn except for the purposes specified in the scheme or, as the case may be, in the deposit scheme.

(4) Notwithstanding anything contained in sub-section (3), no deduction under sub-section (1) shall be allowed in respect of any amount utilised for the purchase of—

(a) any machinery or plant to be installed in any office premises or residential accommodation, including any accommodation in the nature of a guest-house;

(b) any office appliances (not being computers);

(c) any machinery or plant, the whole of the actual cost of which is allowed as a deduction (whether by way of depreciation or otherwise) in computing the income chargeable under the head "Profits and gains of business or profession" of any one previous year;

(d) any new machinery or plant to be installed in an industrial undertaking for the purposes of business of construction, manufacture or production of any article or thing specified in the list in the Eleventh Schedule.

(5) Where any amount standing to the credit of the assessee in the special account or in the Site Restoration Account is withdrawn on closure of the account during any previous year by the assessee, the amount so withdrawn from the account, as reduced by the amount, if any, payable to the Central Government by way of profit or production share as provided in the agreement referred to in section 42, shall be deemed to be the profits and gains of business or profession of that previous year and shall accordingly be chargeable to income-tax as the income of that previous year.

Explanation.—Where any amount is withdrawn on closure of the account in a previous year in which the business carried on by the assessee is no longer in existence, the provisions of this sub-section shall apply as if the business is in existence in that previous year.

(6) Where any amount standing to the credit of the assessee in the special account or in the Site Restoration Account is utilised by the assessee for the purposes of any expenditure in connection with such business in accordance with the scheme or the deposit scheme, such expenditure shall not be allowed in computing the income chargeable under the head "Profits and gains of business or profession".

(7) Where any amount, standing to the credit of the assessee in the special account or in the Site Restoration Account, which is released during any previous year by the State Bank of India or which is withdrawn by the assessee from the Site Restoration Account for being utilised by the assessee for the purposes of such business in accordance with the

scheme or the deposit scheme is not so utilised, either wholly or in part, within that previous year, the whole of such amount or, as the case may be, part thereof which is not so utilised shall be deemed to be profits and gains of business and accordingly chargeable to income-tax as the income of that previous year.

²⁴[***]

(8) Where any asset acquired in accordance with the scheme or the deposit scheme is sold or otherwise transferred in any previous year by the assessee to any person at any time before the expiry of eight years from the end of the previous year in which it was acquired, such part of the cost of such asset as is relatable to the deduction allowed under sub-section (1) shall be deemed to be the profits and gains of business or profession of the previous year in which the asset is sold or otherwise transferred and shall accordingly be chargeable to income-tax as the income of that previous year :

Provided that nothing in this sub-section shall apply

(i) where the asset is sold or otherwise transferred by the assessee to Government, a local authority, a corporation established by or under a Central, State or Provincial Act or a Government company²⁵ as defined in section 617 of the Companies Act, 1956 (1 of 1956); or

(ii) where the sale or transfer of the asset is made in connection with the succession of a firm by a company in the business or profession carried on by the firm as a result of which the firm sells or otherwise transfers to the company any asset and the scheme or the deposit scheme continues to apply to the company in the manner applicable to the firm.

Explanation.—The provisions of clause (ii) of the proviso shall apply only where—

(i) all the properties of the firm relating to the business or profession immediately before the succession become the properties of the company;

(ii) all the liabilities of the firm relating to the business or profession immediately before the succession become the liabilities of the company; and

(iii) all the shareholders of the company were partners of the firm immediately before the succession.

(9) The Central Government may, if it considers necessary or expedient so to do, by notification in the Official Gazette, direct that the deduction allowable under this section shall not be allowed after such date as may be specified therein.

Explanation.—For the purposes of this section,—

(a) "State Bank of India" means the State Bank of India constituted under the State Bank of India Act, 1955 (23 of 1955);

(b) the expression "amount standing to the credit of the assessee in the special account or the Site Restoration Account" includes interest accrued to such accounts.]"

Section 37

"Section 37(1) says that any expenditure (not being expenditure of the nature described in sections 30 to 36 and not being in the nature of capital expenditure or personal expenses of the assessee), laid out or expended wholly and exclusively for the purposes of the business or profession shall be allowed in computing the income chargeable under the head, "Profits and Gains of Business or Profession".

Section 42

Special provision for deductions in the case of business for prospecting, etc., for mineral oil

"42(1) For the purpose of computing the profits or gains of any business consisting of the prospecting for or extraction or production of mineral oils in relation to which the Central Government has entered into an agreement with any person for the association or participation¹ of the Central Government or any person authorised by it in such business] (which agreement has been laid on the Table of each House of Parliament), there shall be made in lieu of, or in addition to, the allowances admissible under this Act, such allowances as are specified in the agreement in relation-

(a) to expenditure by way of infructuous or abortive exploration expenses in respect of any area surrendered prior to the beginning of commercial production by the assessee;

(b) after the beginning of commercial production, to expenditure incurred by the assessee, whether before or after such commercial production, in respect of drilling or exploration activities or services or in respect of physical assets used in that connection, except assets on which allowance for depreciation is admissible under section 32

[Provided that in relation to any agreement entered into after the 31st day of March, 1981, this clause shall have effect subject to the modification that the words and figures "except assets on which allowance for depreciation is admissible under section 32" had been omitted; and]

(c) to the depletion of mineral oil in the mining area in respect of the assessment year relevant to the previous year in which commercial production is begun and for such succeeding year or years as may be specified in the agreement;

and such allowances shall be computed and made in the manner specified in the agreement, the other

provisions of this Act being deemed for this purpose to have been modified to the extent necessary to give effect to the terms of the agreement."

(2) Where the business of the Assessee consisting of prospecting for or extraction or production of petroleum and natural gas is transferred wholly or partly or any interest in such business is transferred in accordance with the agreement referred to in sub-section (1), subject to the provisions of the said agreement and where the proceeds of the transfer (so far as they consist of capital sums)

(a) are less than the expenditure incurred remaining unallowed, a deduction equal to such expenditure remaining unallowed, as reduced by the proceeds of transfer, shall be allowed in respect of the previous year in which such business or interest, as the case may be, is transferred;

(b) exceed the amount of the expenditure incurred remaining unallowed, so much of the excess as does not exceed the difference between the expenditure incurred in connection with the business or to obtain interest therein and the amount of such expenditure remaining unallowed, shall be chargeable to income-tax as profits and gains of the business in the previous year in which the business or interest therein, whether wholly or partly, had been transferred :

Provided that in a case where the provisions of this clause do not apply, the deduction to be allowed for expenditure incurred remaining unallowed shall be arrived at by subtracting the proceeds of transfer (so far as they consist of capital sums) from the expenditure remaining unallowed.

Explanation.—Where the business or interest in such business is transferred in a previous year in which such business carried on by the assessee is no longer in existence, the provisions of this clause shall apply as if the business is in existence in that

previous year;

(c) are not less than the amount of the expenditure incurred remaining unallowed, no deduction for such expenditure shall be allowed in respect of the previous year in which the business or interest in such business is transferred or in respect of any subsequent year or years:

Provided that where in a scheme of amalgamation or demerger, the amalgamating or the demerged company sells or otherwise transfers the business to the amalgamated or the resulting company (being an Indian company), the provisions of this sub-section—

(i) shall not apply in the case of the amalgamating or the demerged company; and

(ii) shall, as far as may be, apply to the amalgamated or the resulting company as they would have applied to the amalgamating or the demerged company if the latter had not transferred the business or interest in the business.

Explanation.—For the purposes of this section, "mineral oil" includes petroleum and natural gas.

6. Section 37(1) of the Act is a residual provision and besides various deductions for business expenditure prescribed under Section 32 to 36 of the Act which are specific in nature, Section 37(1) of the Act provides that any expenditure (not being expenditure of the nature described in sections 30 to 36 and not being in the nature of capital expenditure or personal expenses of the assessee), '**laid out or expended**' '**wholly and exclusively**' for the

purposes of the business or profession shall be allowed in computing the income chargeable under the head "Profits and gains of business or profession". Thus the expenditure incurred by Assessee or a provision made for the same both are allowable under Section 37(1) of the Act, provided such expenditure is incurred wholly and exclusively for the purpose of business and is laid out or expended for the purpose of business.

7. The crux of the matter therefore assumes relevance is whether the 'Provision for Site Restoration' made by the Assessee during the three relevant years viz., Assessment Year 1996-1997, 1997-1998 and 1998-1999 was laid out or expended wholly and exclusively for the purpose of business or not.

8. The Assessee is engaged in the business of oil exploration in India and as per the Product Sharing Contract between The Government of India, Oil and Natural Gas Corporation Limited (ONGC), Videocon Petroleum Limited, Command Petroleum (India) Pte Limited, Ravva Oil (Singapore) Pte Ltd, with respect to contract Area identified as Ravva Oil & Gas Fields. The Assessee Company undertaking such oil exploration was obligated under the Clause 1.77 and 14.9 of the Contract to restore the site by filling up the pits,

after the oil exploration work is over. The said relevant clauses are also quoted below for ready reference:

"1.77. "Site Restoration" shall mean all activities required to **return a site to its natural state or to render a site compatible with its intended after use** (to the extent reasonable, having regard to its former use, if any, and state), after cessation of Petroleum Operations in relation thereto and shall include, where appropriate, proper abandonment of wells or other facilities, removal of equipment, structures and debris, establishment of compatible contours and drainage, replacement of top soil, revegetation, slope stabilisation, infilling of excavations or any other appropriate actions in the circumstances."

"14.9 Contractor's Abandonment Obligations

On expiry or termination of this Contract or relinquishment of part of the Contract Area, the Contractor shall;

(a) Subject to Article 28, remove all equipment and installations from the relinquished area or former Contract Area in a manner agreed with the Government pursuant to an abandonment plan; and

(b) Perform all necessary Site Restoration activities in accordance with good international petroleum industry practice and take all other action necessary to prevent hazards to human life or to the property of others or the environment."

9. The learned counsel for the Assessee Mr.R.V.Easwar, Senior counsel who is also an Ex-Judge of High Court, submitted that the Provisions for such expenditure to be incurred in future for Site Restoration Work made on a scientific and rational basis depending upon the quantum of oil expected to be explored, based on production of the oil which was worked out depending upon the share of the oil of various Companies of which the Assessee had 22.5% of the total oil explored and over the expected production of the oil in barrels and abandonment costs computed by the Company. The Assessee Company computed the said expected liability of site restoration charges and accordingly made provisions for the three assessment years in question and illustratively the computation of the provision for Assessment Years 1997-1998, as explained in the Affidavit filed by the Assessee before this Court on 21.01.2020 is extracted below:

Site restoration charge calculations (FY 1997-98)

S.No.	Particulars	USD
A	Total Abandonment costs estimated in Table 31 of PSC	20,000,000.00
B	Abandonment Costs provided in FY 1995-96	(403,572.21)
C	Abandonment Costs provided in FY 1996-97	(595,963.69)
D	Abandonment Costs left to be provided in USD as on 01/04/97 (A-B-C)	19,000,464.10
E	Reserves left as on 01/04/97	213,070,779.00
F	Abandonment Cost Per Barrell (D/E)	0.09
G	Production During 1997-98	12,857,377.00
H	Provision to be made USD (FXG)	1,146,549.20
I	CEIPL Share @ 22.5% (HX22.5%)	257,973.57
J	CEIPL Share in INR (1X39.397)	10,163,384.69

10. The learned counsel further urged that the Hon'ble Supreme Court in the case of **Calcutta Company Limited Vs. CIT reported in (1959) 37 ITR 1 (SC)**, has laid down that inasmuch as the liability which had accrued during the accounting year, was to be discharged at a future date, the amount to be expended in the discharge of that liability would have to be estimated in order that under the mercantile system of accounting, the amount could be debited before it was actually disbursed. The relevant portion of the said Judgement are quoted below for ready reference:

"Turning now to the facts of the present case, we find that the sum of Rs. 24,809 represented the

*estimated expenditure which had to be incurred by the appellant in discharging a liability which it had already undertaken under the terms of the deeds of sale of the lands in question and was an accrued liability which according to the mercantile system of accounting **the appellant was entitled to debit in its books of account** for the accounting year as against the receipts of Rs. 43,692-11-9 which represented the sale proceeds of the said lands. Even under [s. 10\(2\)](#) of the Income-tax Act, it might possibly be urged that **the word "expended was capable of being interpreted as "expendable "or to be expended "** at least in a case where a **liability to incur the said expenses had been actually incurred by the assessee** who adopted the mercantile system of accounting and the debit of Rs. 24,809 **was thus a proper debit** in the present case. We need not however base our decision on any such consideration. We are definitely of opinion that the sum of Rs. 24,809 represented the estimated amount which would have to be expended by the appellant in the course of carrying on its business and was incidental to the same and having regard to the accepted commercial practice and trading principles was a deduction which, if there was no specific provision for it under [section 10\(2\)](#) of the Act was certainly allowable deduction, in arriving at the profits and gains of the business of the appellant*

under [section 10\(1\)](#) of the Act, there being no prohibition against it, express or implied in the Act."

11. Further relying upon the another Judgment of the Hon'ble Supreme Court in the case of **Bharat Earth Movers Vs. Commissioner of Income-tax** reported in **(2000) 245 ITR 428 (SC)**, the learned counsel for the Assessee submitted that the law is settled: *if a business liability has definitely arisen in the accounting year, the deduction should be allowed although the liability may have to be quantified and discharged at a future date.* The learned counsel for the Assessee also relied upon the Judgment of the Hon'ble Supreme Court in the case of **Metal Box Company of India Ltd. Vs. Their Workmen** reported in **(1969) 73 ITR 53 (SC)**. In paragraphs 4 and 5 of the Judgment in the case of Bharat Earth Movers (supra), the Hon'ble Supreme Court had discussed the ratio of **Metal Box Company of India Ltd. Vs. Their Workmen**, which is quoted below for ready reference:

"4.The law is settled: *if a business liability has definitely arisen in the accounting year, the deduction should be allowed although the liability may have to be quantified and discharged at a future date. What should be certain is the incurring of the liability. It should also be capable of being*

*estimated with reasonable certainty though the actual quantification may not be possible. **If these requirements are satisfied the liability is not a contingent one.** The liability is in praesenti though it will be discharged at a future date. It does not make any difference **if the future date on which the liability shall have to be discharged is not certain.***

5. In **Metal Box Company of India Ltd. Vs. Their Workmen (1969) 73 ITR 53** the appellant company estimated its liability under **two gratuity schemes** framed by the company and the amount of liability was deducted from the gross receipts in the P&L account. The company had worked out on an actuarial valuation its estimated liability and made provision for such liability not all at once but spread over a number of years. The practice followed by the company was that every year the company worked out the additional liability incurred by it on the employees putting in every additional year of service. The gratuity was payable on the termination of an employees service either due to retirement, death or termination of service – **the exact time of occurrence of the latter two events being not determinable with exactitude before hand.** A few principles were laid down by this court, the relevant of which for our purpose are extracted and reproduced as under:-

"(i) For an assessee maintaining his accounts on mercantile system, a liability already accrued, though to be discharged at a future date, would be a proper deduction while working out the profits and gains of his business, regard being had to the accepted principles of commercial practice and accountancy. It is not as if such deduction is paid; permissible only in case of amounts actually expended or

(ii) Just as receipts, though not actual receipts but accrued due are brought in for income-tax assessment, so also liabilities accrued due would be taken into account while working out the profits and gains of the business;

(iii) A condition subsequent, the fulfillment of which may result in the reduction or even extinction of the liability, would not have the effect of converting that liability into a contingent liability; (iv) A trader computing his taxable profits for a particular year may properly deduct not only the payments actually made to his employees but also the present value of any payments in respect of their services in that year to be made in a subsequent year if it can be satisfactorily estimated."

12. The learned counsel for the Assessee further submitted that the three yardsticks, criteria or parameters for allowing the 'Provisions made for future expenditure was discussed by the Hon'ble Supreme Court in the case of **Rotork Controls India (P) Ltd., Vs. Commissioner of Income Tax** reported in **2009 314 ITR 0062**, which is quoted below for ready reference

*"A provision is a liability which can be measured only by using a substantial degree of estimation. A provision is recognized when: (a) an enterprise has a **present obligation** as a result of a past event; (b) it is **probable that an outflow** of resources will be required to settle the obligation; and (c) **a reliable estimate** can be made of the amount of the obligation. If these conditions are not met, no provision can be recognized. Liability is defined as a present obligation arising from past events, the settlement of which is expected to result in an outflow from the enterprise of resources embodying economic benefits. A past event that leads to a present obligation is called as an obligating event. The obligating event is an event that creates an obligation which results in an outflow of resources. It is only those obligations arising from past events existing independently of the future conduct of the business of the enterprise that is recognized as provision. For a liability to qualify for*

*recognition there must be not only present obligation but also the probability of an outflow of resources to settle that obligation. Where there are a number of obligations (e.g. **product warranties or similar contracts**) the probability that an outflow will be required in settlement, is determined by considering the said obligations as a whole."*

13. Thus, the three criteria of the provision is recognized when: (a) an enterprise has a present obligation as a result of a past event; (b) it is probable that an outflow of resources will be required to settle the obligation; and (c) a reliable estimate can be made of the amount of the obligation.

14. The learned counsel for the Appellant urged that all the three criteria are satisfied by the Assessee in the present cases and there is no dispute from the side of the Revenue that the Assessee has incurred an obligation under the contract known as 'Product Sharing Agreement' vide clause 1.77 r/w. Clause 14.9 thereof, quoted above. The question of restoring the site of exploration after the work is over for which the said provision is made is based on a scientific method and relevant materials. He submitted that initial period of the said contract of the Assessee entered into in the year 1994 was 25 years and the same has been recently further extended for the period of ten years on 24.10.2019. Thus, after October

2029, it can be expected that oil exploration work would be over and the Assessee will have to restore the site to its original as nearly as possible, and that expenditure is covered by the provisions made in the present Assessment Years.

15. He further submitted that this claim of the said provision as 'business expenditure' under Section 37 (1) of the Act is only for the present three Assessment Years in question A.Y. 1996-1997, 1997-1998 and 1998-1999 as there is amendment with respect to 33ABA with effect from 01.04.1999 viz A.Y. 1999-2000.

16. Drawing the distinction between the allowability of expenditure under Section 37(1) and 57(iii) of the Act which deals with "Income from Other Sources", the Hon'ble Supreme Court in the case of **Commissioner of Income Tax Vs. Rajendra Prasad Moddy**, reported in (1978) 115 ITR 519 (SC), the Hon'ble Supreme Court quoting the observations from **Lord Thankerton in Hughes Vs. Bank of New Zealand** reported in (1938) 6 ITR 636 held that language under Section 37 (1) of the Act is little wider than that of Sec. 57(iii) and therefore the expenditure should be laid out or expended wholly and exclusively for the purpose of making or earning income chargeable under the Head "Income From Other Source" so as to be

allowable deduction under Section 57(iii) of the Act. The relevant discussion made in paragraph 2 of the Judgment is quoted below for ready reference.

"2.The determination of the question before us turns on the true interpretation of **section 57(iii)** and it would, therefore, be convenient to refer to that section, but before we do so, we may point out that **section 57(iii)** occurs in a fasciculus of sections under the heading 'F- Income From Other Sources'. **Section 56** which is the first in this group of sections enacts in sub-section (1) that income of every kind which is not chargeable to tax under any of the heads specified in **section 14**, Items A to E shall be chargeable to tax under the head 'Income From Other Sources' and sub-section (2) includes in such income various items one of which is 'dividends'. Dividend on shares is thus income chargeable under the head 'Income From Other Sources'. **Section 57** provides for certain deductions to be made in computing the income chargeable under the head "Income From Other Sources" and one of such deductions is that set out in clause (iii) which reads as follows:

"Any other expenditure (not being in the nature of capital expenditure) laid down or expended wholly and exclusively for the purpose of making or earning such income".

The expenditure to be deductible under [section 57\(iii\)](#) must be laid out or expended wholly and exclusively for the purpose of making or earning such income. The argument of the Revenue was that unless the expenditure sought to be deducted resulted in the making or earning of income, it could not be said to be laid out or expended for the purpose of making or earning such income. The making or earning of income, said the Revenue, was a sine qua non to the admissibility of the expenditure under [section 57\(iii\)](#) and, therefore, if in a particular assessment year there was no income, the expenditure would not be deductible under that section. The Revenue relied strongly on the language of [section 37\(1\)](#) and contrasting the phraseology employed in [section 57\(iii\)](#) with that in [section 37\(1\)](#), pointed out that the Legislature had deliberately used words of narrower import in granting the deduction under [section 57\(iii\)](#). [Section 37\(1\)](#) provided for deduction of expenditure laid out or expended wholly and exclusively for the purpose of the business or profession in computing the income chargeable under the head 'Profits or gains of business or profession'. The language used in [section 37\(1\)](#) was "laid out or expended-for the purpose of the business or profession" **and not** "laid out or expended-**for the purpose of making or earning such income**" as set out in [section 57\(iii\)](#). **The**

words in section 57(iii) being narrower, contended the Revenue, they **cannot be given the same wide meaning as the words in section 37(1)** and hence no deduction of expenditure could be claimed under **section 57(iii)** unless it was productive of income in the assessment year in question. This contention of the Revenue undoubtedly found favour with two High Courts **but we do not think we can accept it.** Our reasons for saying so are as follows.

17. The observations of Lord Thankerton in *Hughes* (supra) is apt to be quoted here where the said Law Lord held that "*Expenditure in the course of the trade which is unremunerative is none the less a proper deduction, if wholly and exclusively made for the purposes of the trade. It does not require the presence of a receipt on the credit side to justify the deduction of an expense.*"

18. This said observation came to be applied and invoked in large number of Indian Judgments later on. In paragraph 6 of the Judgment in the case of **Commissioner of Income Tax Vs. Rajendra Prasad Moddy**, reported in **(1978) 115 ITR 519 (SC)**, the Hon'ble Supreme Court had discussed the view of Lord Thankerton in *Hughes* (supra) in the following terms:-

"This view which we are taking is clearly supported by the observations of **Lord Thankerton in Hughes v. Bank of New Zealand** where the learned Law Lord said: "Expenditure in the course of the trade which is unremunerative is none the less a proper deduction, if wholly and exclusively made for the purposes of the trade. It does not require the presence of a receipt on the credit side to justify the deduction of an expense." We find that the same view has been taken by the **Madras High Court in Appa Rao v. Commissioner of Income tax**, and **Mohamed Ghouse v. Commissioner of Income-tax**, the **Bombay High Court in Ormerods (India) Private Ltd. v. Commissioner of Income-tax**, the **Allahabad High Court in Chhail Beharilal v. Commissioner of Income-tax**, the **Madhya Pradesh High Court in Commissioner of Income-tax v. Dr. Fida Hussain G. Abhasi**, the **Kerala High Court in M. N. Ramaswamy Iyer v. Commissioner of Income-tax** and the **Orissa High Court in Commissioner of Income-tax v. Gopal Chand Patnaik**. **This view is eminently correct** as it is not only justified by the language of **section 57(iii)** but it also accords with the principles of commercial accounting. The **contrary view taken by the Patna High Court in Maharajadhiraj Sir Kameshwar Singh v. Commissioner of Income-tax** and the Calcutta High

Court in Madanlal Sohanlal v. Commissioner of Income-tax must in the circumstances be held to be incorrect."

19. Relying upon the aforesaid Judgments, the learned counsel appearing for the Assessee submitted that the Tribunal has erred in disallowing the said expenditure even under Section 37 (1) of the Act without assigning any proper or detailed reason in the impugned order.

20. The words "**Lay (Laid out)**" or "**Expend (Expended)**", as employed in Section 37 (1) of the Act, are defined in the following manner, in the Second Edition of the Oxford English Dictionary published by Clarendon Press-Oxford, in the following manner.

"Expend- To pay out, spend. It differs from spend in being less colloquial, and (in mod.use) in implying some determinate direction or object of outlay.

(a) To put away, lay out, spend (money). To spend, make away with, consume in outlay.

(b) To lay out (money) for determinate objects. Const.in, upon.

Expendable- Also expendible- That may be expended; considered as not worth preserving or salvaging; normally consumed in use; *spec.* of military personnel; that may be allowed to be sacrificed to achieve a military objective. hence as sb., an expendable person or object.

Lay-To put away in store; to store up; to save (money).

-To put away for future disposal or for safety.

-To spend, expend, lay out.

21. These definitions indicate that the words Lay, Laid or Expend do not merely include the immediate expenditure or laying out of the funds, but if they are set apart for a determinate and the specific object also, a future actual expenditure is also included in these terms.

22. On the other hand, the learned counsel for the Revenue Mr.T.Ravikumar merely relied upon the Circular 772 dated 23.12.1999 to explain that a new Section 33ABA has been inserted by Finance Act 1998 in which the emphasis was laid on actual expenditure incurred by the Assessee by way of deposit in the Site Restoration Fund. The learned counsel for the Revenue therefore urged that in the absence of any actual expenditure

incurred during the present three Assessment years such an allowance could not be made in the case of the Assessee.

23. However at this stage itself we make it clear that Section 33ABA is not applicable to the three Assessment years viz., 1996-1997, 1997-1998 and 1998-1999 and the learned counsel for the Assessee himself has stated before us that from 01.04.1999 viz. Assessment Year 1999-2000, the Assessee has not claimed any "Provision" as deduction and the controversy involved is restricted only for these three Assessment years.

24. Secondly the learned counsel for the Revenue relied upon the Judgment of the Hon'ble Supreme Court in the case of **New India Mining Corporation Ltd Vs. Commissioner of Income Tax** reported in **(2000) 243 ITR 640 (SC)** in which case the learned Tribunal has held that the expenditure incurred by the appellant for the purpose of restoring the lease land to the original condition was permissible under Section 37(1) of the Income Tax Act. Further, the Tribunal has found that since no expenditure was incurred by the Assessee therein and therefore, in the Hon'ble Supreme Court has held that once it is held that since no expense was incurred by the appellant, the question of any allowable expense being deducted in computing the income from the profits and gains of the appellant does not

arise. Further, the question of allowability of Provision of such expenditure was not even involved in the said Judgment. Therefore the said Judgment relied upon by the learned counsel for the Assessee is clearly distinguishable and does not advance the case of the Revenue.

25. The learned counsel for the Revenue Mr.T.Ravi Kumar further relied upon the Judgment of **Shri Sajjan Mills Ltd. Vs. Commissioner of Income Tax and another** reported in **(1985) 156 ITR 585 (SC)** in which the Hon'ble Supreme Court held that contingent liabilities do not constitute expenditure and cannot be the subject matter of deduction even under the mercantile system of accounting. Paragraph 24, 25 of the said Judgment is quoted below for ready reference.

*"24.The right to receive the payment accrued to the employees on their retirement or termination of their services and the liability to pay gratuity became the accrued liability of the assessee when the employees retired or their services, were terminated. **Until then the right to receive gratuity is a contingent right and the liability to pay gratuity continues to be a contingent ability qua** the employer. An employer might pay gratuity when the employee retires or his service is terminated and claim the payment made as an expenditure incurred for the purpose of business*

under [section 37](#). **He might, if he followed the mercantile system, provide for the payment of gratuity which became payable during the previous year and claim it as an expenditure on the accrued basis under [section 37](#) of the said Act.** Since the amount of gratuity payable in any given year would be a variable amount depending upon the number of employees who would be entitled to receive the payment during the year, the amount being a large one in one year and a small one in another year, the employer often finds it desirable and/or convenient to set apart for future use a sum every year to meet the contingent liability as a provision for gratuity or a fund for gratuity. He might create an approved gratuity fund for the exclusive benefit of his employees under an irrevocable trust and make contributions to such fund every year. Contingent liabilities do not constitute expenditure and can not be the subject matter of deduction even under the mercantile system of accounting. Expenditure which was deductible for income tax purposes is **towards a liability actually existing at the time but setting apart money which might become expenditure on the happening of an event is not expenditure.** (See in this connection the observations of this Court in [Indian molasses Co. \(P\) Ltd., v. Commissioner of Income-tax, West Bengal](#)),

37 I.T.R. 66 at pages 76 & 80. A distinction is often made between an **actual liability in praesenti and a liability de futuro, which for the time being is only contingent.** The former is deductible but not the latter.

25. Amounts set apart by way of provision or by way of a reserve or fund to meet the liability of gratuity as and when it becomes payable will not be deductible allowance or expenditure. Where, however, an approved gratuity fund is created for the exclusive benefit of the employees under an irrevocable trust, contribution made to the fund during the year of account will be allowed to be deducted under [section 36\(1\)\(v\)](#).

26. The said observation was made by the Hon'ble Supreme Court that the contingent liabilities do not constitute expenditure and cannot be the subject matter of deduction even under the mercantile system of accounting was made in the context of Section 40(A)(7) of the Act which was inserted by Finance Act 1975 with effect from 01.04.1973 and which provides that no deduction shall be allowed in respect of the provisions made by the Assessee for the payment of gratuity to the employees on their retirement or on their termination of employment for any reason. This provision was apparently brought in to undo the Judgment of *Metal Box Company of India*

Ltd supra whereby the Hon'ble Supreme Court allowed the Provision for payment of gratuity. Thus, the said Judgment relied upon by the learned counsel for the Revenue also dealt with the different context in which provisions was made for payment of gratuity to the employees being contingent liability which was not allowable due to specific provisions under Section 40A(7) of the Act. This analogy is akin to the 'Site Restoration Fund' under the provisions brought in the statute book under Section 33ABA. Thus if the Provisions of Act require specific deposit or actual payment of that liability, the Provision made for that may not be allowed, but such is not the position in the case before us. Thus if the Provision of the Act require specific deposit or actual payment of that liability, the Provision made for that may not be allowed, but such is not the position in the case before us.

27. He further relied upon the Judgment of the Karnataka High Court in the case of ***Mysore Lamp Works Ltd. Vs. Commissioner of Income Tax*** reported in **(1990) 185 ITR 0096 (Kar)**. In the said Judgment, the Karnataka High Court had dealt with the case of payment of bonus to the workmen under the provisions of Bonus Act 1965 and it held that the Expenditure which is deductible for income-tax purposes, is one which is towards a liability actually existing at the time, but the putting aside the money which may become expenditure on the happening of an event is not

expenditure. This Judgment is also, with great respects, not applicable to the facts of the present case inasmuch as the liability to restore the site in question incurred by the Assessee in the present case is a contractual obligation incurred by the Assessee under the Product Sharing Contract, which is a multi-party agreement and the above fact is not disputed by the Revenue.

28. The learned counsel for the Revenue also placed reliance on the Judgment of the Madras High Court in the case of **Renowned Auto Products Mfrs. Ltd Vs. Income Tax Officer** reported in **(2013) 354 ITR 127 (Mad)** where the Co-ordinate Bench of this Court held that where the provisions of warranty costs was not created on scientific basis and such provision seemed just an ascertained contingent liability, the same was not deductible under Section 37 (1) of the Act. The said aspect was already discussed in the Judgment of **Rotork Controls India (P) Ltd., Vs. Commissioner of Income Tax** reported in **(2009) 314 ITR 0062 (SC)**, and therefore the Judgment of **Renowned Auto Products Mfrs. Ltd.** (supra) is not applicable to the facts of the present case, as we find that the Provisions for 'Site Restoration' in the present case was made by the Assessee on a Scientific, Rational and reasonable computing basis, and it was not on ad-hoc basis.

29. Thus on the conspectus of the legal precedents discussed above, we are of the clear opinion that for the three Assessment Years in question, the provision made by the Assessee for 'Site Restoration cost' under the contractual obligations of the Assessee in the Product Sharing Contract, made on scientific basis was clearly an allowable expenditure under Section 37(1) of the Act. The only ingredient required to be complied with for Section 37(1) of the Act is that the expenditure in question should be laid out or expended wholly for the purpose of business of the Assessee. There is no dispute that the Provision in question was made wholly and exclusively for the purpose of business. The only dispute was that expenditure not actually incurred in these years and the amount was to be spent in future out of the Provision made during these Assessment years namely A.Y.1996-1997 to 1998-1999.

30. We find no prohibition or negation for making a provision for meeting such a future obligation and such a provision being treated as a revenue expenditure under Section 37(1) of the Act. The Hon'ble Supreme Court in the case of **Calcutta Company Limited** clearly held that the words Lay (laid out) or Expend includes expendable in future also, which has been quoted by us above. The making of a Provision by an Assessee is a

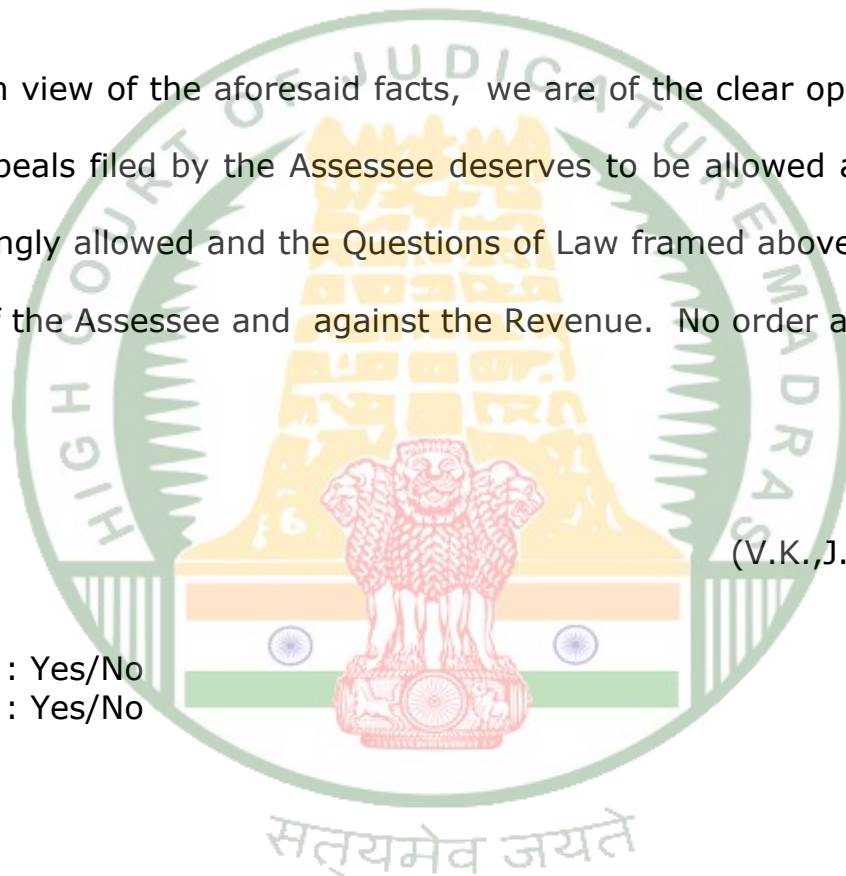
matter of good business or commercial prudence and it is to set apart a fund computed on scientific basis to meet the expenditure to be incurred in future. There is no time frame or limitation prescribed for the said provisions to be actually spent. Merely because in the context like the one involved in this case, the contract period was long viz., 25 years, which too now stands extended by period of ten years or more and therefore the actual work of site restoration may happen after 35 years depending upon the actual exploration of oil reserves and the Site restoration would be undertaken only if there is no longer some oil to be explored or drawn out and, therefore, it cannot be said that the provision made for the three Assessment Years presently at the beginning of the Contract period was irrational or an disallowable expenditure. The question of commercial expediency is a usual business and the economic decision to be taken by the Assesee and not by the Revenue Authorities and therefore the provision made on a reasonable basis, cannot be disallowed under Section 37(1) of the Act, unless it can be said to be have no connection with the business of the Assesee. The words wholly and exclusively for the purpose of business is a sufficient safeguard and check and balance by the Revenue Authorities to test and verify the creation of provisions for meeting a liability by the Assessee in future and its connectivity with the business of the Assessee. Assuming that such set apart provision is not actually spent in future or

something less is spent on Site Restoration, nothing prevents Revenue Authorities and Assessee himself to offer it back for taxation in such future year, the unspent Provision to be brought back to tax as per Section 41(1) of the Act.

31. In view of the aforesaid facts, we are of the clear opinion that the present Appeals filed by the Assessee deserves to be allowed and the same are accordingly allowed and the Questions of Law framed above are answered in favour of the Assessee and against the Revenue. No order as to costs.

(V.K.,J.) (R.S.K.,J.)
23.01.2020

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DR. JUSTICE VINEET KOTHARI,J
and
MR. JUSTICE SURESH KUMAR,J

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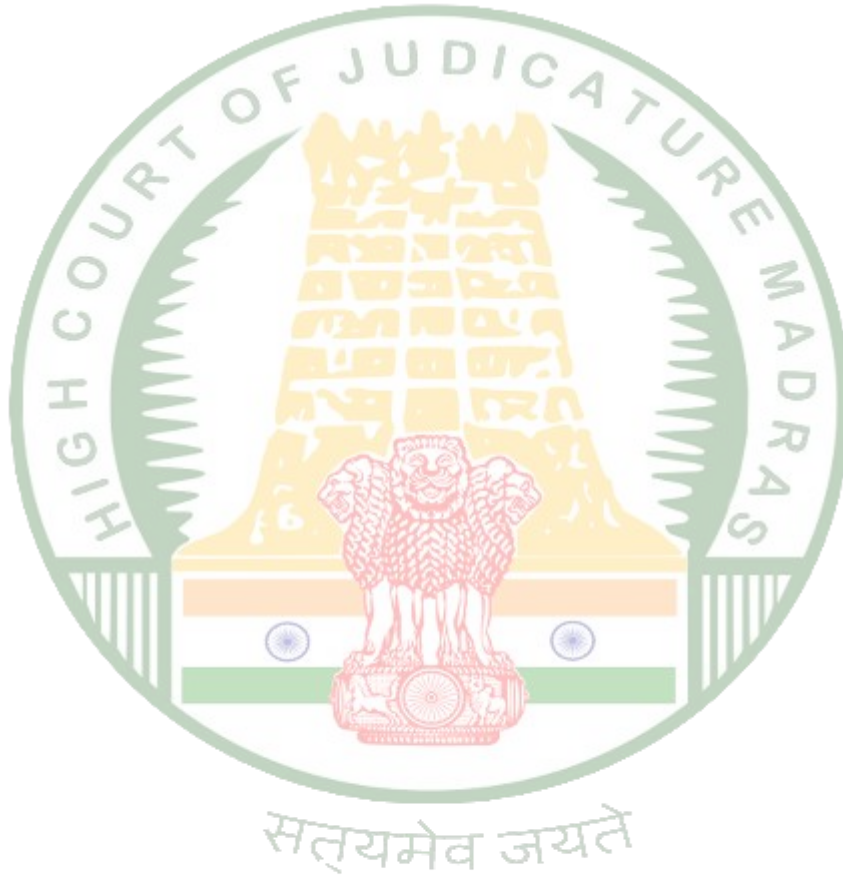
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