[2023] 13 S.C.R. 371 : 2023 INSC 917

CASE DETAILS

C.I.T., DELHI

v.

BHARTI HEXACOM LTD.

(Civil Appeal No. 11128 of 2016)

OCTOBER 16, 2023

[B.V. NAGARATHNA AND UJJAL BHUYAN, JJ.]

HEADNOTES

Issues for consideration:

Whether the variable annual licence fee paid by the respondents-assessees to the Department of Telecommunications (DoT) under the New Telecom Policy of 1999 is revenue expenditure in nature and is to be allowed deduction under Section 37 of the Income Tax Act, 1961, or, the same is capital in nature and is accordingly required to be amortised under Section 35ABB of the Act; and Whether the High Court of Delhi was right in apportioning the licence fee as partly revenue and partly capital by dividing the licence fee into two periods, that is, before and after 31st July, 1999 and accordingly holding that the licence fee paid or payable for the period upto 31 July, 1999 i.e. the date set out in the Policy of 1999 should be treated as capital and the balance amount payable on or after the said date should be treated as revenue.

Income Tax Act, 1961 – ss. 35ABB and 37– The New Telecom Policy, 1999 – Variable licence fee paid to DoT under the New Telecom Policy of 1999 – Revenue Expenditure or Capital Expenditure – Nature of :

Held: 1. In considering whether an item of expenditure is of a capital or revenue nature, one must consider the nature of the concern, the ordinary course of business usually adopted in that concern and the object with which the expenditure is incurred. Attention must be paid not only to the form of the transaction, but also its substance. What is material is the nature of right sought to be secured through the payment or transaction in question. The purpose towards which the expenditure is incurred must guide any attempt to categorise the expenditure. The structure or form of the transaction or the payment schedule is hardly suggestive of the nature of the transaction. Therefore, it cannot be axiomatically held that an expenditure which in its core, capital in nature, is actually to be treated as a revenue expenditure simply because the payment is structured in installments. The determinative test to identify whether an expenditure structured in the form of instalments is in the nature of a capital expenditure or revenue expenditure, would be to first assess whether the payment made either in lump-sum or in instalments relates to the acquisition or expansion of a capital asset, or by contrast, relates to the working of an asset to produce profits; whether the consideration payable towards the acquisition or expansion of a capital asset has simply been chopped up into smaller sums payable in instalments, for the sake of convenience. The annual payment of variable licence fee is only towards licence fees and merely because it is paid in annual instalments based on the Adjusted Gross Revenue (AGR), the payment cannot be construed as revenue. The annual payments of licence fee as also the entry fee relate to a singular purpose, i.e., the acquisition of the right to carry on the business of rendering telecommunication services. This right being in the nature of a capital asset, any payment(s) made towards the acquisition of the right, whether in lump-sum or in annual instalments dependent on the AGR, would be in the nature of capital disbursement(s). Where the periodic payments are referrable to or have a nexus with the original obligation undertaken by the assessee as consideration for acquisition of a right, the periodic payments would be in the nature of capital expenditure, notwithstanding the fact that they are payable as a percentage of profits, gross revenue or sales. In the present case, since the entry fee as well as variable licence fees are traceable to the same source, they would both have to be held to be capital in nature, notwithstanding the fact that the variable licence fee is paid in a staggered manner. [Paras 22, 22.1, 22.2, 23.3, 23.4 and 24]

2. The payment of entry fee as well as the variable annual licence fee paid by the respondents-assessees to the DoT under the Policy of 1999 are capital in nature and may be amortised in accordance with Section 35ABB of the Act. The High Court of Delhi was not right in apportioning the expenditure incurred towards establishing, operating and maintaining telecom services, as partly revenue and partly capital by dividing the licence fee into two periods, that is, before and after 31 July, 1999 and accordingly holding that the licence fee paid or payable for the period upto 31 July, 1999

i.e. the date set out in the Policy of 1999 should be treated as capital and the balance amount payable on or after the said date should be treated as revenue. The nature of payment being for the same purpose cannot have a different characterisation merely because of the change in the manner or measure of payment or for that matter the payment being made on annual basis. In the ultimate analysis, the nomenclature and the manner of payment is irrelevant. The payment post 31 July, 1999 is a continuation of the payment pre 31 July, 1999 albeit in an altered format which does not take away the essence of the payment. It is a mandatory payment traceable to the foundational document i.e., the license agreement as modified post migration to the 1999 policy. Consequence of non-payment would result in ouster of the licensee from the trade. Thus, this is a payment which is intrinsic to the existence of the licence as well as trade itself. Such a payment has to be treated or characterized as capital only. [Paras 26 and 27]

Tax / Taxation: Expenditure – Whether a given expenditure is capital or revenue in nature – Determination of – Principles and Tests – Considerations which are immaterial in determining the question – Discussed. [Paras 19 and 21]

Tax / Taxation – Classification of expenditure or receipts – Difficulty of relying on a single precedent for purpose of classification – Precedent.

Held: The propositions made in earlier cases, if sought to be applied to a different case which the authors of those propositions did not have in mind, could lead to absurd results. It is trite that the words in a judgment must not be construed in the same manner as those in a legislation. Hence, it is neither wise nor suitable to extend the dictum of one case, premised on the facts of the said case, to another fact-situation which is seemingly similar but not really so. This is particularly so when there is no precedent which has been rendered in an identical fact situation, as is the case in the instant matters. [Para 23]

Tax / Taxation: Capital assets – Depreciation and Amortisation – One of the exceptions to depreciation of capital assets is amortisation – Income Tax Act, 1961 – ss.35A, 35AB, 35ABA and 35ABB.

Held: Amortisation is a form of depreciation, however, the distinction between the two being that in the case of depreciation, an asset may be depreciated progressively, and may even be exhausted before the lifetime expectancy of the asset in question, whereas, in the case of amortisation, the value of the asset gets progressively depleted, matching with the expected timeframe of the right. [Para 10.3]

Royalty – Distinction between payment made to acquire a right, and payment of royalty for use of a right or asset – Discussed. [Para 20]

LIST OF CITATIONS AND OTHER REFERENCES

Jonas Woodhead and Sons Ltd. v. Commissioner of Income Tax (1997) 224 ITR 342; *CIT, Madras v. Best and Co. (Pvt.) Ltd.* (1966) 60 ITR 11; *Southern Switch Gear Ltd. v. CIT* (1998) 232 ITR 359 and *CIT v. Sarada Binding Works,* (1976) 102 ITR 187- held inapplicable.

Alembic Chemical Works Co. Ltd. v. CIT (1989) 3 SCC 329 : [1989] 2 SCR 302 and *Mewar Sugar Mills Ltd. v. CIT,* (1973) 3 SCC 143 : [1973] 2 SCR 429 – distinguished.

Empire Jute Co. Ltd. v. Commissioner of Income Tax (1980) 124 ITR 1; *Assam Bengal Cement Co. Ltd. v. CIT, West Bengal* (1955) 27 ITR 34; *CIT v. Jalan Trading Co. Pvt. Ltd.* (1985) 4 SCC 59 : [1985] 2 Suppl. SCR 517; *Pingle Industries Ltd. v. CIT* (1960) 40 ITR 67 (SC); *L.H. Sugar Factory and Oil Mills Pvt. Ltd. v. Commissioner of Income Tax, U.P.,* (1980) 125 ITR 293; *M/s. Devidas Vithaldas and Co. v. C.I.T., Bombay City* (1972) 3 SCC 457 : [1972] 3 SCR 215; *Commissioner of Income Tax, Bombay City I v. CIBA India Ltd.,* (1968) 69 ITR 692 (SC); *Travancore Sugars and Chemicals Ltd. v. Commissioner of Income-tax,* (1966) 62 ITR 566 and *India Cements v. Commissioner of Income Tax,* 60 I.T.R. 52 (SC) – relied on.

Board of Agricultural Income Tax, Assam v. Sindhurani Chaudurani (1957) 32 ITR 169; *Enterprising Enterprises v. Deputy Commissioner of Income Tax,* (2007) 293 ITR 437; *Aditya Minerals Pvt. Ltd. v. Commissioner of Income Tax* (1999) 8 SCC 97 : [1999] 2 Suppl. SCR 233; *Sundaram Finance Ltd. v. State of Kerala* [1966] 2 SCR 828; *CIT, Bangalore v. J.H. Gotla,* A.I.R. 1985 SC 1698; *Gotan Lime v. CIT,* (1999) 239 ITR 718; and *CIT v. Modi Revlon Pvt. Ltd.,* 2012 SCC OnLine Del 4463 – referred to.

The City of London Contract Corporation Ltd. v. Styles, (1887) 2 TC 239; *Vallambrosa Rubber Co. Ltd. v. Farmer* (1910) 5 T.C. 529; *Ounsworth (Surveyor of Taxes) v. Vickers Ltd.* (1915) 3 K.B. 267; *British Insulated Helsby Cables Ltd. v. Atherton,* (1926) AC 205; *Henriksen v. Grafton Hotel Ltd.,* (1942) 24 T.C. 453; *John Smith & Son v. Moore,* (1921) 12 T.C. 266; *Mallet v. Staveley Coal and Iron Co.,* (1928) 2 K.B. 405; *Anglo-Persian Oil Co. v. Dale* (1932) 1 K.B. 124; *Van Den Berghs, Limited v. Clark (H.M. Inspector of Taxes)* (1935) 19 T.C. 390; *Robert Addie & Sons Collieries Ltd. v. Commissioners of Inland Revenue* (1924) 8 T.C. 671; *Sun Newspapers Limited and the Associated Newspapers Limited v. The Federal Commissioner of Taxation* (1938) 61 C.L.R. 337; *CIR v. Adam,* (1928) 14 T.C. 34; *Bonner v. Basset Mines Ltd.,* (1912) 6 T.C. 145; *Rolfe v. Wimpy Waste Management Ltd.,* (1989) 62 T.C. 399; *Tucker v. Granada Motorway Services Ltd.,* (1979) 53 T.C. 92; *Lawson v. Johnson Matthey Plc.,* (1992) 65 T.C. 39; Dale; *CIR v. Carron Company,* (1968) 45 T.C. 18; *Heather v. PE Consulting Group Ltd.,* (1972) 48 T.C. 293; *Walker v. The Joint Credit Card Co.,* (1982) 55 T.C. 617; *CIR v. Nchanga Copper Mines* (1964) 1 All ER 208;*Commissioners of Inland Revenue v. Ramsay,* 20 T.C. 79; *Inland Revenue v. Williams,* 11 ITR Suppl. 84; *Prendergast v. Cameron,* 8 I.T.R. Suppl. 75 (HL).- referred to.

Tata HydroElectric Agencies Ltd., Bombay v. Commissioner of Income-tax, (1937) L.R. 64 IndAp 215; *Mohanlal Hargovind of Jubbulpore v. Commissioner of Income Tax,* (1949) L.R. 76 IndAp 235;*S Commissioner of Income Tax, Bombay v. Century Spinning, Weaving and Manufacturing Co.,* (1942) 10 ITR Suppl., *Benarsidas Jagannath,* In re, (1946) 15 ITR 185- referred to.

Wheatcroft's treatise on The Law of Income Tax, Sur Tax and Profits Tax – referred to.

OTHER CASE DETAILS INCLUDING IMPUGNED ORDER AND APPEARANCES

CIVIL APPELLATE JURISDICTION: Civil Appeal No. 11128 of 2016.

From the Judgment and Order dated 19.12.2013 of the High Court of Delhi at New Delhi in ITA No.1336 of 2010.

With

Civil Appeal Nos.4902 of 2022, 162 of 2018, 159 of 2021, 4839 of 2017, 153 of 2021, 6897 of 2018, C.A. Diary No. 4178 of 2019, SLP (C) Nos. 24740, 20863 of 2019, Civil Appeal Nos.158, 302, 303 of 2021, 11149, 11148, 11130, 11131, 11134, 11132, 11136, 11133, 11135, 11137, 11140, 11141, 11139, 11142, 11143, 11145, 11146, 11147 of 2016, 163 of 2018, 11129 of 2016 And C.A. Diary No. 24728 of 2023.

Appearances:

N Venkatraman, A.S.G., Arijit Prasad, Sr. Adv., V.C Bharati, Ms. Shruti ShivKumar, Rahul VijayaKumar, Ms. Amritha C. Mouli, Raj Bahadur Yadav, Rupesh Kumar, Mrs. Gargi Khanna, Rajesh Kumar Singh, Vikrant Yadav, S A Haseeb, Manish Pushkarna, Mrs. Anil Katiyar, Advs. for the Appellant.

Arvind P. Datar, Ajay Vohra, Arvind Datar, Sr. Advs., Ms. Kavita Jha, Vaibhav Kulkarni, Udit Naresh, Mahesh Agarwal, Ms. Sayaree Basu Mallik, Abhinav Garg, Sachit Jolly, Ms. Anuradha Dutt, Ms. Disha Jham, Ms. Soumya Singh, Ms. B. Vijayalakshmi Menon, Harpreet Singh Ajmani, Aniket Deepak Agrawal, E. C. Agrawala, Advs. for the Respondent.

JUDGMENT / ORDER OF THE SUPREME COURT

JUDGMENT

NAGARATHNA, J.

Delay condoned.

2. Leave granted.

3. The judgment of the Division Bench of the High Court of Delhi, dated 19 December, 2013 in ITA No. 1336 of 2010 and connected matters, whereby the High Court of Delhi, confirming the decision of the Income Tax Appellate Tribunal, New Delhi (hereinafter, "Tribunal" for short) has held that the variable licence fee paid by the respondents-assessees under the New Telecom Policy, 1999 ((hereinafter referred to as "Policy of 1999" for the sake of convenience), is revenue expenditure in nature and is to be deducted under Section 37 of the Income Tax Act, 1961 (hereinafter referred to as "the Act" for the sake of brevity) is assailed in these appeals. Some of these appeals also arise from judgments passed by the High Courts of

Bombay and Karnataka, following the judgment of the Division Bench of the High Court of Delhi, dated 19 December, 2013.

4. Since common questions of law and facts arise in these appeals, they have been clubbed together and heard and disposed of by this common judgment.

Bird's eye view of the controversy:

5. The controversy in these cases revolves around the question, as to, whether, the variable licence fee paid by the respondent-assessees to the Department of Telecommunications (hereinafter referred to as "DoT", for short) under the New Telecom Policy of 1999 (Policy of 1999) is revenue expenditure in nature and is to be allowed deduction under Section 37 of the Act, or, whether the same is capital in nature, Section 35ABB of the Act.

Brief facts of the case:

6. The National Telecom Policy of 1994 was substituted by the New Telecom Policy of 1999 dated 22 July, 1999. The said Policy of 1999 stipulated that the licencee would be required to pay a one-time entry fee and additionally, a licence fee on a percentage share of gross revenue. The entry fee chargeable would be the fee payable by the existing operator upto 31 July, 1999, calculated upto the said date and adjusted upon notional extension of the effective date. Subsequently, w.e.f. 01 August, 1999, licence fee was payable on a percentage of Annual Gross Revenue ("AGR", for short) earned. The quantum of revenue share to be charged as licence fee was to be finally decided after obtaining recommendation of the Telecom Regulatory Authority of India ("TRAI") but in the meanwhile, the Government of India fixed 15% of the gross revenue of the licencee as provisional licence fee. On receipt of TRAI's recommendation by the Government, adjustment of the dues was to be made.

6.1. Clause 7 of the Policy of 1999 stipulated that upon migration thereto, the licencees would forego the right of operating in a regime of limited number of operators as per the existing licensing agreement and would operate in a multiple licence regime, that is, additional licences without any limit could be issued in a given service area. The period of licence was stated to be twenty years from the effective date of the existing licence agreement, that is, the 1994 Agreement. Migration to the Policy of

1999 was on the condition and premise that the conditions should be accepted as a package in entirety and simultaneously and all legal proceedings shall be withdrawn and no dispute relating to the period upto 31 July, 1999 shall be raised at any future date. If all the terms were accepted, amendments to the existing licence agreement would be signed. The respondents herein migrated to the Policy of 1999. They had paid licence fee upto 31 July, 1999. The respondents treated the licence fee paid upto to 31 July, 1999 that is, the one-time licence fee as stipulated in the letter/communications dated 22 July, 1999, as capital expenditure.

6.2. The respondent companies which are engaged in the business of telecommunication services have procured licences in different telecom circles. Initially, the said licences were given under a licence agreement executed in the year 1994 for a period of ten years subject to expansion of one year or more at the discretion of the authorities. The said licence was non-transferable and non-assignable. In case, there was a breach of any term of the licence or default in payment, the licence could be revoked after providing sixty days' notice. The licence gave the right to operate the services within a geographical area on a non-exclusive basis and the authorities would have the right to modify the conditions of the licence as explained in Schedule A and Schedule B of the licence agreement, in the interest of general public or for security considerations. The schedules pertained to the area of service, tariff ceiling etc.

6.3. In the above backdrop, for the sake of convenience, the specific facts of the lead matter, Civil Appeal No. 11128 of 2016 shall be narrated hereinunder:

Pursuant to the request of the respondent-assessee, a licence was granted to it, *inter-alia* on certain terms and conditions to establish, maintain and operate cellular mobile services. Accordingly, having accepted the Policy of 1999 and migrated thereto, after paying the licence fee upto 31 July, 1999, i.e., the one-time licence fee as stipulated in the Communication dated 22 July, 1999, the respondent-assesee continued in the business of cellular telecommunication and associated value added services, under the regime governed by the Policy of 1999.

6.4. The respondent-assessee filed its return of income on 01 November, 2004 for the assessment year 2003-2004 declaring nil income. The same was processed under Section 143(1) of the Act on 30 March, 2006. The case was selected for scrutiny and a notice was issued to the respondent-assessee under Section 143(2) of the Act, on 20 October, 2005.

6.5. It was noted that an amount of Rs. 11,88,81,000/-, which was the licence fee paid by the assessee on revenue sharing basis, was claimed by the respondent-assessee as revenue expenditure. In that regard, vide questionnaire dated 15 November, 2006, the assessee was required to explain as to why the said amount may, instead, be treated as capital expenditure and amortised over the remaining licence period of twelve years. The respondent-assessee furnished its response to the questionnaire, on 04 December, 2006. On consideration of the assessee's response, an Assessment Order was passed on 27 December, 2006 observing that the amount of Rs. 11,88,81,000/-, i.e. the licence fee paid by the assessee on revenue sharing basis, which was claimed as a revenue expense, ought to have instead been amortised over the remainder of the licence period, i.e., twelve years. Accordingly, an amount of Rs. 99,06,750/- was allowed as a deduction under Section 35ABB of the Act and the remaining amount of Rs. 10,89,74,250/- was disallowed and added back to the income of the respondent-assessee.

6.6. Being aggrieved, the respondent-assessee filed an appeal before the Commissioner of Income Tax (Appeal), New Delhi. In view of the decision of the Commissioner of Income Tax (Appeal) in the assessee's own case for the assessment year 2003-2004, it was reaffirmed vide order dated 27 September, 2007 that the annual licence fee calculated on the basis of annual gross revenue of the assessee would be revenue expenditure deductible under Section 37 of the Act.

6.7. Aggrieved by the said order, the appellant-Revenue preferred an appeal before the Tribunal, New Delhi. By order dated 24 July, 2009, the Tribunal dismissed the Revenue's appeal following its earlier order dated 29 May, 2009 in ITA No. 5335 (Del)/2003 in the case of ***Bharti Cellular Ltd.,*** for the assessment year 2000-2001, the facts of which case were held to be identical to the facts of the case at hand. Being aggrieved, the Revenue filed an appeal before the High Court of Delhi.

6.8. Before the High Court, the Revenue made the following submissions:

That the respondents were granted a licence under the agreement executed under the Indian Telegraph Act, 1885 (hereinafter referred to as the "Telegraph Act" for the sake of brevity). This agreement stated that the licence was granted on certain terms and conditions to establish, maintain and operate cellular mobile services. That the significance of the words "establish, maintain and operate" in the original licence cannot be lost sight of under the Telecom Policy of 1999. The nature and character of the licence fee was not changed. What was changed was only the method of computation. That the assessees had accepted the licence fee payable under the 1994 Agreement as a capital expenditure. They cannot now dispute the same under the Policy of 1999. That under the Policy of 1994, from the fourth year onwards, the assessee had to pay a fixed sum per hundred subscribers. The only change that was made was in the measure, namely, that under the Policy of 1999, the amount was modified to 15% of the gross revenue, but the nature and character of the payment was the same. That mere payment of an amount in instalments did not convert or change the capital payment to a revenue payment. That in order to acquire the right to operate telecom services, obtaining of licence was a sine qua non. The term of the licence was twenty years from the date of commencement and therefore the expenditure is in the nature of capital expenditure.

6.9. *Per contra*, the contention of the assessee before the High Court was that the licence fee payable under the Policy of 1999 was in the nature of revenue expenditure. This was because the earnings are shared and the licence fee depends upon the gross revenue and is payable yearly. That the new operators under the Policy of 1999 were issued licences and were required to pay a one-time licence fee for entry and to start operations and in addition, yearly turn over based licence fee was payable. One-time payment of licence fee was capital expenditure in nature but yearly payable licence fee was revenue expenditure. It was a running expense for maintaining and operating the business of telecommunication and therefore, considered in the commercial sense, the yearly payment was in the nature of revenue expenditure.

6.10. Since the Tribunal had held that variable licence fee paid by the assessees was properly deductible as revenue expenditure, the substantial question of law raised by the High Court at the instance of appellant Revenue was, ***"whether the variable licence fee paid by the respondents under the Telegraph Act, and Indian Wireless Telegraphy Act, 1933 payable under the New Telecom Policy 1999 or 1994 Agreement, is revenue expenditure or capital expenditure which is required to be amortized under Section 35ABB of the Act?"***

The pertinent observations of the High Court and the salient aspects discussed in the judgment dated 19 December, 2013 are as under:

i. Section 35ABB applies when expenditure of a capital nature is incurred by an assessee for acquiring a right for operating telecommunication services. It is immaterial whether the expenditure is/was incurred before or after commencement of the business to operate telecommunication services but what is material is that the payment should be actually made. That Section 35ABB is not a deeming provision but comes into operation and is effective when the expenditure itself is of a capital nature and is incurred towards acquiring a right to operate telecommunication services or for the purposes of obtaining a licence for the said services. That Section 35ABB does not help in determining and deciding the question, as to, whether licence fee paid under the Policy of 1999 or under the 1994 Agreement, was/is capital or revenue in nature.

ii. That there was no decision of the Supreme Court or any of the High Courts directly applicable to the factual matrix of the case and therefore, it would be useful to consider a number of decisions of this Court including, ***Empire Jute Co. Ltd. vs. Commissioner of Income Tax, (1980) 124 ITR 1 ("Empire Jute Co. Ltd."); Assam Bengal Cement Co. Ltd. vs. CIT, West Bengal, (1955) 27 ITR 34 ("Assam Bengal Cement Co. Ltd."); Board of Agricultural Income Tax, Assam vs. Sindhurani Chaudurani, (1957) 32 ITR 169 ("Sindhurani"); Enterprising Enterprises vs. Deputy Commissioner of Income Tax, (2007) 293 ITR 437 ("Enterprising Enterprises").***

iii. Having referred to the aforesaid decisions, three other judgments were noticed by the Delhi High Court which, according to learned ASG appearing for the appellant-Revenue were wrongly applied to the case at hand. The said judgments are, ***Jonas Woodhead and Sons Ltd. vs. Commissioner of Income Tax, (1997) 224 ITR 342 ("Jonas Woodhead and Sons"), Southern Switch Gear Ltd. vs. CIT, (1998) 232 ITR 359 ("Southern Switch Gear Ltd."); CIT, Madras vs. Best and Co. (Pvt.) Ltd., (1966) 60 ITR 11 ("Best and Co.").***

iv. After considering all of the aforesaid judgments, the Delhi High Court in paragraph 29 discerned the facts of the present case as under:

"29. When we turn to the facts of the present case, the following position emerges:

i. The licence was issued under a statutory mandate and was required and acquired, before the commencement of operations or business, to establish and also to maintain and operate cellular telephone services.

ii. The licence was for initial setting up but, thereafter for maintaining and operating cellular telephone services during the term of the licence.

iii. Contrary to what was stated, under the licence agreement executed in 1994 the considerations paid and payable were with the understanding that there would be only two players who would have unfettered right to operate and provide cellular telephone service in the circle. The payment, therefore, had element of warding off competition or protecting the business from third party competition.

iv. Under the 1994 agreement, the licence was initially for 10 years extendable by one year or more at the discretion of the Government/authority.

v. 1994 Licence was not assignable or transferable to a third party or by way of a sub-licence or in partnership. There was no stipulation regarding transfer or issue of shares to third parties in the company.

vi. Under the 1994 agreement, the licencee was liable to pay fixed licence fee for first 3 years. For 4th year and onwards, the licencee was liable to pay variable licence fee @ Rs. 5,00,000/- per 100 subscribers or part thereof, with a specific stipulation on minimum licence fee payable for 4th to 6th year and with modified but similar stipulations from 7th year onwards.

vii. The licence could be revoked at any time on breach of the terms and conditions or in default of payment of consideration by giving 60 days' notice.

viii. The authority also reserved the right to revoke the licence in the interest of public by giving 60 days' notice.

ix. Under 1999 policy, the licencee had to forego the right of operating in the regime of limited number of operators and agreed to multiparty regime competition where additional licences could be issued without limit.

x. There was lock in period on the present shareholding for a period of 5 years from the date of licence agreement i.e. the effective date and even transfer of shareholding directly or indirectly through subsidiary or holding company, was not permitted during this period. This had the effect of 'modifying' or clarifying the 1994 agreement, which was silent.

xi. Licence fee calculated as a percentage of gross revenue was payable w.e.f. 1 August, 1999. This was provisionally fixed at 15% of the gross revenue of the licensee but was subject to final decision of the Government about the quantum of revenue share to be charged as licence fee after obtaining recommendation of the Telecom Regulatory Authority of India (TRAI).

xii. At least 35% of the outstanding dues including interest payable as on 31 July, 1999 and liquidated damages in full, had to be paid on or before 15 August, 1999. Dates for payments of arrears were specified.

xiii. Past dues upto 31 July, 1999 along with liquidated damages had to be paid as stipulated in the 1999 policy, on or before 31 January, 2000 or earlier date as stated.

xiv. The period of licences under 1999 policy was extended to 20 years starting from the effective date.

xv. Failure to pay the licence fee on yearly basis would result in cancellation of licences. Therefore, to this extent licence fee was/is payable for operating and continuing operations as cellular telephone operator."

v. On a consideration of the aforesaid aspects, the Delhi High Court held that the payment of licence fee was capital in part and revenue in part and that it would not be correct to hold that the whole fee was capital or revenue in nature in its entirety. It was further observed that the licencees/assessees in question required a licence in order to start or commence business as cellular telephone operators; that payment of a licence fee was a precondition for the assessees to commence or set up the business. That it was a privilege granted to the assessee subject to payment and compliance with the terms and conditions. For immediate reference, paragraph Nos.31 to 36 of the said judgment are extracted as under:

"**31.** Licence fee under the 1994 agreement ensured that there would be only two private operators in a circle and thus their limited monopoly would be protected and competition by way of third-party private players was warded off. Restricted monopoly of the licencees was ensured. The licence fee fixed included an element towards the said right of the licencees. 1994 agreement, for first three years postulated a lump-sum payment irrespective of number of subscribers. Minimum fee was also prescribed for later years. It appears that licencees were unable to make payments as per the 1994 agreement and under the 1999 policy, were required to pay lump-sum payment for past arrears before specified dates.

32. There was restriction under the 1994 agreement, on transfer of the licence or even grant sub-licence but there was no specific restriction on change of shareholding. 1999 policy ensured that even shareholding did not change for a period of 5 years from the effective date. The effect of acquiring the licence has been examined in paragraph 15 above. The licence was not assignable or transferrable as such, but induction of share capital, transfer of shares etc. was permitted subject to conditions in the 1999 policy. In commercial sense the licence constituted and continues to be the most valuable right which the company has and possesses. Thus, the payment made is for acquiring the licence which is essential and mandatory, prerequisite for establishing the business and for operations or continuance and running of business. Yet, as observed below, it cannot be equated with one time entry fee which a person has to pay to establish the business. It therefore, represents composite payment, both capital and revenue.

33. The licence fee was imposed and payable under the Indian Telegraph Act and other statutory provisions and was/is mandatory. Failure to pay the same would/will result in discontinuance or stoppage of business operations. Under 1999 policy, the amount payable speaks of sharing of gross revenue earned by the service provider from the customers. 1994 agreement as noticed did have a provision for sharing but with minimum payment stipulation. In case of non-payment of licence fee, the licence could be revoked and licencee was not permitted to carry on and continue cellular telephone service. Thus, the licence fee payable was/is equally with the objective and purpose to maintain and operate cellular telephone services. It was also an operating expense and non payment can lead to cancellation as one of the consequences. Endurement requires current expenses and is subject to payment on revenue share. It will not be correct to hold or propound that entire payment during the term of licence, is deferred capital payment. This was/is not the intent under the 1994 agreement or 1999 policy. The intent is to also share the gross earning to maintain and operate the licence.

34. The licence fee as such is similar to both prospecting fee, acquisition of right to lease as well as leases which enabled removal of sand/tendu leaves, etc. as nothing has to be won over, or extracted. Part payment was towards an initial investment which an assessee had to make to establish the business. It was a precondition to setting up of business. It has element and includes payment made to acquire the ‘asset’ i.e. the right to establish cellular telephone service. But the licence permits and allows the assessee to maintain, operate and continue business activities. Payment of licence fee has certain ingredients and is like lease rent which is payable from time to time to be able to use the licence.

35. The licence acquired was initially for 10 years and the term was extended under the 1999 policy to 20 years but this itself does not justify treating the licence fee paid on revenue sharing basis under the 1999 policy as a capital expense made to acquire an asset. As observed in *Empire Jute Co. Ltd.* (supra), the enduring benefit test has limitation and cannot be mechanically applied without considering the commercial or business aspects. Practical and pragmatic view and considerations rather than juristic classification is the determinative factor. The payment of yearly licence fee on revenue sharing basis is for carrying on business as cellular telephone operator. It is a normal business expense.

36. Read in this manner, the licence granted by the Government/ authority to the assessee would be a capital asset, yet at the same time, the assessee has to make payment on yearly basis on the gross revenue to continue, to be able to operate and run the business, it would also be revenue in nature. Failure to make stipulated revenue sharing payment on yearly basis would result in forfeiting the right to operate and in turn deny the assessee, right to do business with the aid of the capital asset. Non-payment will prevent and bar an assessee from providing services."

vi. In paragraph 36, it was observed that the licence granted by the Government or the concerned authority to the assessee would be a capital asset and yet, since the assessee had to make the payment on a yearly basis on the gross revenue to continue to be able to operate and run the business, it would also be in the nature of revenue expenditure. Having opined thus, the High Court decided to apportion the licence fee as partly revenue and partly capital and divided the licence fee into two periods, that is, before and after 31 July, 1999 and observed that the licence fee that had been paid or was payable for the period upto 31 July, 1999 i.e. the date set out in the Policy of 1999, should be treated as capital expenditure and the balance amount payable on or after the said date should be treated as revenue expenditure. The reasons for the same were stipulated in paragraphs 43 to 46 of the said judgment which reads as under:

"43. Licence fee was payable for establishment, maintenance and operation of cellular telephone service. Establishment and set up took place in the initial years and thereafter the payments made were/are for operation or maintaining the cellular telephone service. Initial outlay and payment, therefore, is capital in nature, whereas the outlays and payments made subsequently are to operate and maintain the service. 1999 policy in the form of letter dated 22 July, 1999 also refers to one time entry fee which is chargeable and had to be calculated as licence fee dues payable upto 31 July, 1999 and licence fee was thereafter payable on percentage share of gross revenue. The new licences issued to others also stipulated one time entry fee and then licence fee payment on sharing basis. In view of the new 1999 policy, the earlier policy which restricted competition, underwent a change and licencees forgo their right to operate in the regime of limited number of operators. Another reason why we feel that licence fee payable for the period on or before 31 July, 1999 should be treated as capital and the amount payable thereafter as revenue, is justified and appropriate in view of Section 35ABB. We have already quoted the said section above. The provision provides that licence fee of capital nature shall be amortized by dividing the amount by number of remainder years of licences. Thus, the capitalized amount of licence fee is to be apportioned as a deduction in the unexpired period of the licence. The provision will have ballooning effect with amortized amount substantially increasing in the later years and in the last year the entire licence fee alongwith the brought forward amortized amount would be allowed as deduction. After a particular point of time, deduction allowable under Section 35ABB would be more than the actual payment by the assessee as licence fee for the said year. This would normally happen after the mid-term of the licence period. Section 35ABB, therefore, ensures that the capital payment is duly allowed as a deduction over the term and once the expenditure is allowed, it would be revenue or tax neutral provided the tax rates remain the same during this period.

44. ITA Nos. at serial Nos. 1 to 9 above primarily relate to variable licence fee, which is to be shared under the 1999 Policy whereas, ITA No. 417/2013 filed against Hutchison Essar Ltd. relates to the period of variable licence fee payable for the fourth year under the 1994 Agreement.

45. The effect thereof is that we are treating about 20% of the expenditure in terms of the tenure as per the 1999 Policy as capital in nature, whereas if we apply the 1994 Agreement, we would be treating about 40% of the expenditure as per the tenure as payable towards establishing or setting up of cellular business. By the time 1999 Policy was implemented in the case of the respondents-assessees, the cellular telephone business had already commenced and was in operation. The 1999 Policy had the effect of extending period of licence from 10 years to 20 years, but from the effective date. The view, we have taken, effectively means that the entire licence fee paid in the initial first four years is treated as capital in nature i.e. the expenditure incurred to establish cellular telephone business, whereas the balance expenditure payable on year to year basis from 5 year onwards is treated as revenue expenditure to run and operate cellular telephone business.

46. However, we would like to discuss two judgments relied upon by Huthison Essar Pvt. Ltd. in support of their contention that the variable fee even prior to 31 July, 1999 should be treated as revenue expenditure. As noted above, this was the 4 year and the contention of the assessee is that in this year even as per the 1994 agreement, payment had to be made on revenue sharing basis subject to the minimum guarantee. Learned counsel for the assessee had relied upon CIT v. Sharda Motors Industry Ltd. (supra). In the said case reference was made to J.K. Synthetics Ltd. (supra) to hold that no substantial question of law arises. The Revenue had relied upon Southern Switch Gear Ltd. v. CIT (1998) 232 ITR 359 (SC), but the said judgment was distinguished on the ground that lump-sum royalty was paid and 25% thereof was disallowed by the tribunal on the ground that it was capital payment. In Sharda Motor Industries Ltd. (supra), royalty was to be paid on quantity of goods produced calculated per piece. However, this does not appear to be sole basis why the payment made was treated as

revenue expenditure. The court had relied upon other facts which are noticed in paragraph 3 of the same judgment i.e. the payment was made for running business. The question of apportionment and payment was not made to establish business. In CIT v. Modi Revlon (P.) Ltd. (2012) 26 Taxmann.com 133 (Delhi), a Division Bench of this High Court observed that the tests evolved over the period have disapproved the applicability of the 'once and for all' payment and more structured approach which would take into account several factors like the licence tenure; whether licence created further rights; whether there was restriction for use of confidential information; whether benefits were transferred once and for all; whether after expiry of the licence, plans and drawings were to be returned, etc. As held and observed above, it is nature and object for which the payment is made which determines the character of payment. In the said case, it was observed that there was nothing to show or to suggest vesting of knowhow in the assessee and therefore, the assessee did not derive any enduring benefit. Thus, the royalty payment was held to be revenue in nature."

In view of the above discussion, the substantial question was answered by the High Court in the following manner:

"47. In view of the aforesaid findings, the substantial question mentioned above in item Nos. 1 to 9 is answered in the following manner:

(i) The expenditure incurred towards licence fee is partly revenue and partly capital. Licence fee payable upto 31 July, 1999 should be treated as capital expenditure and licence fee on revenue sharing basis after 1 August, 1999 should be treated as revenue expenditure.

(ii) Capital expenditure will qualify for deduction as per Section 35ABB of the Act.

48. The appeal ITA No. 417/2013 by the Revenue in the case of Hutchison Essar Pvt. Ltd., pertains to the assessment year 1999-2000 i.e. year ending 31 March, 1999. It is for the period prior to the period 31 July, 1999. As per the discussion above, the licence fee payable on or before 31 July, 1999 should be treated as capital expenditure

> and the licence fee payable thereafter should be treated as revenue expenditure. In view of the aforesaid position, the question of law admitted for hearing in this appeal as recorded in the order dated 21 August, 2013, has to be answered in favour of the revenue and against the respondent assessee."

6.11. Aggrieved by the aforesaid reasoning and conclusions arrived at by the High Court of Delhi in its judgment dated 19 December, 2013, which has been followed by High Courts of Delhi, Bombay and Karnataka, the appellant-Revenue has preferred these appeals.

Submissions:

7. We have heard the learned Additional Solicitor General of India (ASG), Sri N. Venkataraman for the Revenue and learned senior counsel Sri Ajay Vohra, Sri Arvind Datar and learned counsel Sri Sachit Jolly, for the respondent-assessees and perused the material placed on record.

Submissions on behalf of the appellant-Revenue:

7.1. Learned ASG, at the outset, submitted that the judgment of the High Court of Delhi dated 19 December, 2013 is incorrect inasmuch as it has sought to dissect the payment of licence fee to hold that the entry fee paid in the initial four years ought to be treated as capital expenditure and amortised accordingly, while the fee payable on an annual basis from the fifth year onwards, as a percentage of the gross revenue of the assessees was treated as revenue/business expenditure. It was further contended as follows:

i. That the schedule of payment cannot recharacterize the transaction under income tax law, particularly when this Court had laid down from time to time that the schedule of payment, whether lump-sum or periodical, is immaterial in determining its classification under income tax law. The payment(s) towards the same purpose, i.e., payment of licence fee, cannot be characterised partly as capital and partly as revenue in nature by artificially defining one part as an entry fee and the remainder, payable annually, when both types of payment was towards licence fees.

ii. That when the respondent-assessees have duly amortised the licence fee paid annually as capital expenditure, under the 1994 licence regime as well as the entry fee under the Policy of 1999 regime, there was no basis to reclassify the same as revenue expenditure insofar as variable licence fee is concerned for the subsequent years. Variable payments made annually, based on the annual gross revenue in the relevant year were also towards licence fee. Therefore, there could not have been a shift in the tax treatment thereof upon migration to a new regime, wherein merely the payment schedule was revised while preserving the character of the payment.

iii. That payments made, either of entry fee or of annual licence fee, is in essence only towards securing a licence to establish, maintain or operate a telegraph i.e. system. If either of the aforesaid payments is not made, or short paid, the licence would be revoked under Section 8 of the Telegraph Act. Further, Section 4 of the said Act authorises the Government to grant licence against a consideration. Therefore, both entry fee as well as annual licence fee are included within the ambit of 'consideration' chargeable under Section 4. Hence, any submission that licence fee should be split into two components, namely, entry fee for acquiring the licence and variable licence fee for operating the licence, has no legal basis. Such a fragmentation is neither statutorily permissible, nor prescribed in the licence agreement.

iv. Referring to Section 35ABB of the Act, which allows amortisation of expenditure incurred for obtaining a licence to operate telecommunication services, it was contended that the said provision applies in relation to payments made for "acquiring any right to operate telecommunication services" whether such payment was made "before the commencement of the business to operate or thereafter at any time during the previous year." In view of the aforesaid expression, the mode and manner of payment becomes irrelevant. As long as the payment is towards licence fee, the expenditure so incurred will be "in the nature of capital expenditure" as envisaged under Section 35ABB of the Act.

v. That the expression "either before the commencement of the business to operate or thereafter" is also found in Section 35ABA of the Act which pertains to the right to use Spectrum, similar to Section 35ABB which relates to licence to operate telecommunication services. The legislative intent is therefore clear that both these rights would flow from the Central Government on payment, and further, the payment would be partly lump-sum and partly in a deferred manner, considering the nature of rights acquired.

vi. Reliance was placed on the decision of a Constitution-Bench of this Court in ***Aditya Minerals Pvt. Ltd. vs. Commissioner of Income Tax, (1999) 8 SCC 97 ("Aditya Minerals Pvt. Ltd.")*** to assert that the law laid down therein is that as long as payment is towards a capital expenditure, it is immaterial whether it is paid in lump-sum or as periodical payments, or, as a combination of both. That the mode of payment will not be determinative in identifying the nature of the expenditure, i.e., as to whether it is capital or not.

vii. That the decision of this Court in ***Assam Bengal Cement Co. Ltd.*** has clarified that the aim and object of the expenditure would determine the character thereof, while the source and manner of payment would have no consequence.

viii. Referring to the cases of ***Jonas Woodhead and Sons, Southern Switch Gear Ltd.*** and ***Best and Co.,*** which have been referred to by the High Court of Delhi in the impugned judgement, it was submitted that reliance on the said cases is misplaced inasmuch as the said cases did not deal with a single source/purpose towards which payments in different forms had been made. On the contrary, in the said cases, the purpose of payments was traceable to different subject matters and accordingly, this Court held that the payments could be apportioned. However, in the present case, the licence issued under Section 4 of the Telegraph Act is a single licence to establish, maintain and operate telecommunication services. Since it is not a licence for divisible rights which conceives of divisible payments, apportionment of the licence fee by holding that the entry fee paid is towards establishment and therefore, capital, while the licence fee paid as a percentage of gross revenue is towards operation and maintenance and therefore, Revenue, is without legal basis.

ix. Reliance was placed on the decision of this Court in ***CIT vs. Jalan Trading Co. Pvt. Ltd., (1985) 4 SCC 59 ("Jalan Trading Co.")*** to submit that in the said case this Court had an occasion to consider an annual payment in the form of profit sharing towards the right to carry on business. That in the said case, this Court concluded that the annual payment of 75% profit share would still be a payment that was capital in nature, as the same was paid as consideration under a deed of assignment for the right to carry on business. That this judgement will squarely apply to the facts of the present case since the annual payment based on AGR is only towards licence fees and merely because it is paid on the annual gross revenue, the payment cannot be construed as a revenue expenditure.

With the aforesaid submissions, it was prayed that these appeals filed by the Revenue be allowed and the impugned judgments of the High Courts of Delhi, Bombay and Karnataka, following the judgment of the Division Bench of the High Court of Delhi dated 19 December, 2013, be set aside and it be declared that the annual payment is in the nature of a capital expenditure.

7.2. *Per contra*, learned senior counsel, Sri Ajay Vohra, appearing on behalf of the respondent-assessees in Civil Appeal No. 11130 of 2016, supported the judgment of the Division Bench of the High Court of Delhi dated 19 December, 2013 and submitted that the said judgment was passed based on a correct appreciation of the facts of the case and the law and therefore, the same would not call for any interference by this Court. It was further submitted as follows:

i. That on a bare reading of the said provision and the mode of amortisation of expenses, it is patently clear that the same would be applicable only if the following cumulative conditions are satisfied:

a) the expenditure is capital in nature;

b) the expenditure is incurred by an assessee on acquisition of the right to operate telecom services;

c) the expenditure represents payment actually made to obtain a licence.

Thus, for attracting the provisions of Section 35ABB, it is necessary that the expenditure under consideration must be capital in nature and is incurred for acquiring or obtaining a licence, which gives the right to the assessee to operate telecom services.

ii. That in the present case, the respondent-assessees had obtained the licence in the year 1994 and had thereafter set up the telecommunication infrastructure and started operating telecommunication services. The payment of licence fee under the fixed regime, i.e., prior to migration to the Policy of 1999 was for obtaining the licence, thereby resulting in the acquisition of the right to operate telecommunication services. Therefore, the fixed licence fee upto 31 July, 1999 was amortised and allowed in terms of Section 35ABB of the Act. On the other hand, the variable licence fee payable w.e.f. 01 August, 1999, is a percentage of the AGR. The same is not in the nature of capital expenditure as it is not incurred with a view to acquire the right to operate telecommunication services. The said services were already being operated by the respondents by virtue of a licence which had been obtained in the year 1994. The variable licence fee was, thus, for continuing the right to operate telecommunication services, which were already being operated and provided by the respondent-assessees.

iii. Referring to the salient features of the Policy of 1999, it was submitted that the said policy made a paradigm shift by making qualitative changes in licence conditions. It facilitated the entry of new players on payment of one-time entry fee and variable revenue share. The policy document highlights and emphasises the distinction between a one-time fee which is the payment for obtaining the licence, on the one hand and the variable licence fee, which is payment made on a recurring basis based on revenue share, for continuing the right to operate telecommunication services. Therefore, the one-time entry fee to be paid by a new entrant obtaining a licence post 31 July 1999 is required to be amortised under section 30ABB of the Act while the variable licence fee payable as a revenue share would be admissible business expenditure or revenue deduction.

iv. That the Policy of 1999 has not only changed the mechanism of payment but also modified the rights accruing under the licence already obtained vide the original agreement dated 29 November 1994, in lieu of the payment of variable licence fee. The tenure of the licence was increased from ten to twenty years; the licence fee was bifurcated into two parts, i.e., fixed entry fee paid for obtaining the licence and variable annual licence fee paid for continuing with the licence. Thereby the whole complexion of the consideration provided under the original agreement, was changed. That, since the restriction of the number of players or operators in each region was completely lifted, coupled with the fact that variable licence fee was to be paid on an annual basis, in order to continue with the right to operate telecommunication services, no enduring benefit was accruing to the respondent-assessees. Neither was there any monopoly right, nor would the licence remain valid and subsist for an indefinite period of time. The licence would be valid only so long as the annual payment of variable licence fee was made.

v. That the provisions of Section 35ABB of the Act were introduced in the year 1996. At that time, the concept of variable licence fee did not exist. Application of the said provision to variable licence fee would give rise to absurd results, not intended by the Legislature.

vi. That payment of variable licence fee from 01 August, 1999 is not for "acquiring any right to operate telecommunication services", which right vested in and was being exploited by the assessees pursuant to obtaining the licence in 1994 and setting up the requisite infrastructure.

vii. Further, variable licence fee paid from 01 August, 1999 could not be regarded as payment made "to obtain a licence", so as to fall within the ambit of Section 35ABB of the Act.

That Section 35ABB of the Act would not be attracted in the present case to require amortisation of the variable licence fee, because:

a) payment of variable licence fee is not in the nature of capital expenditure;

b) such payment is not incurred for "acquiring any right to operate telecommunication services";

c) such payment has not been made "to obtain a licence".

With the aforesaid submissions, it was prayed that the High Courts' decision as to the inapplicability of Section 35ABB of the Act, to the facts of the present case, be upheld, and these appeals be dismissed as being devoid of merit.

7.3. Learned senior counsel, Sri Arvind P. Datar, appearing on behalf of some of the respondent-assessees in Civil Appeal Nos. 11131 of 2016 and 153 of 2021 adopted the submissions of Sri Ajay Vohra and further submitted as under:

i. That it would be incorrect to suggest that the annual licence fee which is paid as a percentage of the revenue earnings is paid to acquire the right and obtain the licence. That it is absurd to state that every year, each telecom licencee acquires the right and obtains a licence. Acquisition of the right and obtaining the licence is a one-time event and the expenditure for acquisition of the licence is always capital expenditure. Section 35ABB of the Act covers this aspect of the transaction.

ii. That the annual licence fee, even though termed as a licence fee is in essence, expenditure incurred to operate the telecommunication services from year to year. Such expenditure is incurred annually to earn revenue and consequently is an annual revenue expenditure. In various sectors, such as mining, oil exploration, etc., the licences are acquired on payment of a lump-sum amount. This expenditure is to acquire a right and obtain licence to engage in mining, oil exploration, and so on. Thereafter, annual amounts are paid, depending on the quantities of minerals or petroleum that is extracted. It was submitted that by analogy, the one-time entry fee paid by existing telecom operators and the entry fee that was paid by all the new entrants, was capital expenditure which resulted in acquisition of rights and obtaining licence. However, the annual licence fee, which varied according to the AGR in the relevant year, was incurred annually on revenue earned and consequently is an annual revenue expenditure.

iii. Referring to the decision of this Court in ***Mewar Sugar Mills Ltd. vs. CIT, (1973) 3 SCC 143 ("Mewar Sugar Mills Ltd."),*** it was submitted that in the said case, the expenditure incurred by the assessee was apportioned and it was held that the sums paid by the assessee for acquisition of monopoly rights for manufacture of sugar were in the nature of capital expenditure, while the royalty paid on a yearly basis was revenue expenditure. It was submitted in that context that the principle laid down in the said case would directly apply to the case at hand. The one-time entry fee is payed for acquiring the licence and is therefore in the nature of capital expenditure; whereas, the annual licence fee is to operate the licence and earn profits, therefore, the same is revenue expenditure.

iv. That a similar view was taken in ***CIT vs. Sarada Binding Works, (1976) 102 ITR 187 ("Sarada Binding Works")*** wherein the Madras High Court considered various judgments of this Court and held that a lump-sum payment to acquire a right would be capital expenditure, whereas any amount paid as royalty based on annual earnings or profit would be revenue expenditure. That the payment of annual licence fee, in the present case, would be similar to the payment of royalty as it relates to the annual turnover and would therefore be revenue in nature.

v. That it could not be axiomatically held that the nomenclature 'annual licence fee' would itself indicate that the annual variable licence fee was also incurred for the purpose of acquiring the capital asset, i.e., the licence and therefore, had to be amortised under Section 35ABB of the Act. The nomenclature does not mean that a licence is acquired annually or the licence is obtained annually. This amount is the expenditure incurred to operate the telecom licence and earn revenue or profits. In this regard, reliance was placed on the dictum of this Court in ***Sundaram Finance Ltd. vs. State of Kerala, (1966) 2 SCR 828*** to submit that the use of a particular expression is not conclusive of the nature of a transaction.

vi. That the judgment of this Court in **Jalan Trading Co.,** sought to be relied upon by the appellant-Revenue would have no application to the facts of the present case as unlike in the case at hand, there was no lump-sum payment in the said case. The agreement itself provided for 75% of the net profits to be paid for the assignment of the right to carry on business. The aim or object of payment of the said consideration was for the purpose of acquiring the right to carry on business. However, in the present case, the annual licence fee is paid not to acquire the licence, but to operate the telecom licence and earn revenue or profits. Hence, the decision of this Court in ***Jalan Trading Co.***, turns on its own facts.

7.4. Sri Sachit Jolly, learned counsel appearing for the respondent-assessees in Civil Appeal No. 4902 of 2022 adopted the submissions of learned senior counsel, Sri Ajay Vohra and Sri Arvind P. Datar and further contended as follows:

i. That merely because the DoT can rescind the licence owing to non-payment of the variable licence fee, it does not mean that the payment of such fee is towards the acquisition of the licence. Violation of other conditions of licence like non-maintenance of KYC of subscribers could also lead to cancellation of licence. In fact, payment of licence fee for any one year, neither leads to acquisition of any new asset nor to any enduring benefit. Further, the benefit, if any, of the variable licence fee is only restricted to one year to which the payment pertains. Hence, the same could not be held to be capital expenditure or expenditure incurred for acquisition of a capital asset.

ii. That the interpretation sought to be canvassed by the appellant would result in a completely absurd result wherein the deduction under Section 35ABB would exceed the actual payment made by the assessee in a given year, in the later years. This aspect of the matter was rightly appreciated by the Delhi High Court in the impugned judgement and it was accordingly held that the interpretation proposed by the appellant would give Section 35ABB a ballooning effect with the amortised amount substantially increasing in the later years and in the last year, the entire licence fee along with the brought forward, amortised amount would be allowed as deduction. It was rightly held that after a certain point of time, deduction allowable under Section 35ABB would be more than the actual payment made by the assessee as licence fee for that year.

In this context, reliance was placed on the decision of this Court in ***CIT, Bangalore vs. J.H. Gotla, A.I.R. 1985 SC 1698*** to contend that it is settled law that an interpretation which leads to an absurd result should be avoided and such interpretation should give way to a more harmonious interpretation so that the legislation is given its desired result.

iii. With the aforesaid submissions, it was stated that the impugned decision of the High Court of Delhi is detailed and well-reasoned. It is not contrary to any principle laid down by this Court and hence does not merit interference. It was prayed that the appeals filed by the Revenue be dismissed on the ground that there is no infirmity in the impugned judgment of the High Court of Delhi.

Reply arguments:

8. By way of reply, learned ASG, Sri N. Venkataraman, reiterated his submissions while also contending that the judgment of this Court in ***Mewar Sugar Mills Ltd.*** and the judgment of the Madras High Court in ***Sarada Binding Works,*** relied upon by Sri Datar to substantiate the claim that the same source of expenditure incurred by an assessee could be construed as partly capital and partly revenue would not come to the aid of the respondents-assessees in the present case. In this regard, it was further submitted as follows:

i. That in both the aforesaid cases sought to be relied upon by Sri Datar, a single source of expenditure was not split partly as capital and partly as revenue expenditure. On the contrary, in both of those decisions, this Court examined two different constituents of expenditure and held one to be capital and the other to be revenue in nature.

ii. That in ***Sarada Binding Works*** the facts were that the agreement in question envisaged conveyances of two distinct aspects: first, the right to run the business of Chandamama Publications for a consideration of a fixed sum of Rs.5000/- per annum; second, royalty on the sales equivalent to 10% of the net profit of each year of business. The High Court's judgment categorically records that annual payments based on the turnover had no nexus with the payment made to acquire the right to carry on trade, which was also paid annually at Rs.5000/- every year. However, in the facts of the present case, the entry fee as well as the annual licence fee payable as a percentage of AGR, are both towards the same purpose, i.e., acquisition of licence to carry on telecommunication operator services.

iii. That similarly, in the case of ***Mewar Sugar Mills Ltd.,*** two different payments were made, relatable to two different subject matters. In the said judgment, this Court noted that the payment of royalty based on quantity of sugar manufactured, was not with a view to acquire monopoly rights. In the said case, there were two clearly discernible purposes towards which the payment of lump-sum consideration and payment of royalty were made. However, in the present case, the purpose of payment of entry fee as well as the annual licence fee, is singular, i.e., to acquire and retain the right to carry on the business of rendering telecommunication services.

In light of the aforesaid submissions, Sri N. Venkataraman urged that this Bench may allow the appeals filed by the Revenue.

Points for consideration:

9. Having heard the learned counsel for the respective parties and on perusal of the material on record, the following points would emerge for our consideration:

i. Whether the variable annual licence fee paid by the respondents-assessees to the DoT under the Policy of 1999 is revenue in nature and is to be allowed deduction under Section 37 of the Act, or, the same is capital in nature and is accordingly required to be amortised under Section 35ABB of the Act?

ii. Whether the High Court of Delhi was right in apportioning the licence fee as partly revenue and partly capital by dividing the licence fee into two periods, that is, before and after 31st July, 1999 and accordingly holding that the licence fee paid or payable for the period upto 31 July, 1999 i.e. the date set out in the Policy of 1999 should be treated as capital and the balance amount payable on or after the said date should be treated as revenue?

iii. What order?

Statutory Framework:

10. The statutory scheme and structure of the Act on the characterisation of capital expenditure is as follows:

10.1. Section 32 of the Act identifies tangible and intangible assets which are capital in nature and prescribes the mode and manner of depreciation. Section 32(1)(i) identifies a list of tangible assets and Section 32(1)(ii), a set of intangible assets which includes licences. Explanation 3 to Section 32(1) defines 'assets' into two categories, i.e., tangible and intangible. Licences are identified as intangible assets and are therefore, capital in nature.

10.2. Any capital asset is depreciable in terms of Section 32 of the Act, unless specifically dealt with elsewhere. One of the exceptions to depreciation of capital assets is amortisation. Sections 35A, 35AB, 35ABA and 35ABB form one cluster of exceptions wherein, the capital assets referred to in the relevant sections have to be amortised in the manner and mode prescribed therein.

10.3. Amortisation is a form of depreciation, however, the distinction between the two being that in the case of depreciation, an asset may be depreciated progressively, and may even be exhausted before the lifetime expectancy of the asset in question, whereas, in the case of amortisation, the value of the asset gets progressively depleted, matching with the expected timeframe of the right.

10.4. A brief overview of the provisions of the Act which provide for amortisation as a prescribed method, is as under:

i. Section 35A of the Act provides for amortisation of expenditure incurred on acquisition of patent rights or copyright which are intangible assets.

ii. Section 35AB of the Act prescribes the method of amortisation in the case of acquisition of know-how.

iii. Section 35ABA of the Act prescribes the method of amortisation of expenditure incurred on obtaining the right to use spectrum.

iv. Section 35ABB of the Act provides for amortisation of the expenditure incurred for obtaining a licence to operate telecommunication services.

11. At this juncture, it would be useful to reproduce Section 35ABB (1) of the Act, which reads as under:

"35ABB. Expenditure for obtaining licence to operate telecommunication services.—

(1) In respect of any expenditure, being in the nature of capital expenditure, incurred for acquiring any right to operate telecommunication services either before the commencement of the business to operate telecommunication services or thereafter at any time during any previous year and for which payment has actually been made to obtain a licence, there shall, subject to and in accordance with the provisions of this section, be allowed for each of the relevant previous years, a deduction equal to the appropriate fraction of the amount of such expenditure.

Explanation.—For the purposes of this section,—

(i) "relevant previous years" means,—

(A) in a case where the licence fee is actually paid before the commencement of the business to operate telecommunication services, the previous years beginning with the previous year in which such business commenced;

(B) in any other case, the previous years beginning with the previous year in which the licence fee is actually paid,

and the subsequent previous year or years during which the licence, for which the fee is paid, shall be in force;

(ii) "appropriate fraction" means the fraction the numerator of which is one and the denominator of which is the total number of the relevant previous years;

(iii) "payment has actually been made" means the actual payment of expenditure irrespective of the previous year in which the liability for the expenditure was incurred according to the method of accounting regularly employed by the assessee."

(2) Where the licence is transferred and the proceeds of the transfer (so far as they consist of capital sums) are less than the expenditure incurred remaining unallowed, a deduction equal to such expenditure remaining unallowed, as reduced by the proceeds of the transfer, shall be allowed in respect of the previous year in which the licence is transferred.

(3) Where the whole or any part of the licence is transferred and the proceeds of the transfer (so far as they consist of capital sums) exceed the amount of the expenditure incurred remaining unallowed, so much of the excess as does not exceed the difference between the expenditure incurred to obtain the licence 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 licence has been transferred.

Explanation.—Where the licence is transferred in a previous year in which the business is no longer in existence, the provisions of this sub-section shall apply as if the business is in existence in that previous year.

(4) Where the whole or any part of the licence is transferred and the proceeds of the transfer (so far as they consist of capital sums) are not less than the amount of expenditure incurred remaining unallowed, no deduction for such expenditure shall be allowed

under sub-section (1) in respect of the previous year in which the licence is transferred or in respect of any subsequent previous year or years.

(5) here a part of the licence is transferred in a previous year and sub-section (3) does not apply, the deduction to be allowed under sub-section (1) for expenditure incurred remaining unallowed shall be arrived at by—

(a) subtracting the proceeds of transfer (so far as they consist of capital sums) from the expenditure remaining unallowed; and

(b) dividing the remainder by the number of relevant previous years which have not expired at the beginning of the previous year during which the licence is transferred.

(6) Where, in a scheme of amalgamation, the amalgamating company sells or otherwise transfers the licence to the amalgamated company (being an Indian company),—

(i) the provisions of sub-sections (2), (3) and (4) shall not apply in the case of the amalgamating company; and

(ii) the provisions of this section shall, as far as may be, apply to the amalgamated company as they would have applied to the amalgamating company if the latter had not transferred the licence.

(7) Where, in a scheme of demerger, the demerged company sells or otherwise transfers the licence to the resulting company (being an Indian company),—

(i) the provisions of sub-sections (2), (3) and (4) shall not apply in the case of the demerged company; and

(ii) the provisions of this section shall, as far as may be, apply to the resulting company as they would have applied to the demerged company if the latter had not transferred the licence.

(8) Where a deduction for any previous year under sub-section (1) is claimed and allowed in respect of any expenditure referred to in that sub-section, no deduction shall be allowed under sub-section

(1) of section 32 for the same previous year or any subsequent previous year.

11.1. Section 35ABB of the Act governs the treatment of expenditure incurred by entities to obtain a licence for operating telecommunication services in India. The provision addresses the tax treatment of such expenses and ensures that they align with the income tax framework. With effect from 1 April 1996, this provision provides for amortisation of capital expenditure incurred for acquisition of any right to operate telecommunication services, regardless of whether such cost is incurred before the commencement of such business or thereafter. The cost is allowed to be amortised in equal instalments in the years for which the licence is in force. The amortisation commences from the year in which such business commences (where such cost is incurred before the commencement of such business) or the year in which such cost is actually paid, irrespective of the method of accounting adopted by the assessee for such expenditure.

11.2. In order for Section 35ABB of the Act to be applicable, the following cumulative conditions specified in Section 35ABB (1) of the Act are to satisfied:

First, the expenditure must be capital in nature;

Second, the expenditure must be incurred by an assessee for the purpose of acquisition of the right to operate telecom services;

Third, the expenditure must represent the payment actually made to obtain a licence.

Thus, for attracting the provisions of Section 35ABB, it is necessary that the expenditure under consideration must be capital in nature and is incurred for acquiring or obtaining a licence which gives the right to the assessee to operate telecommunication services. Section 35ABB of the Act operates and is effective when the expenditure itself is of a capital nature and is incurred for acquiring a right to operate telecommunication services or is made to obtain a licence for the said services.

Further, the definitions of “relevant previous years”, “appropriate fraction” and “payment has actually been made” have been given by way of an Explanation for the purpose of this Section. Sub-section (2) to (5) deal with deduction to be made accordingly when a licence is transferred and the proceeds of the transfer (so far as they consist of capital sums) are less than or exceed the expenditure incurred remaining unallowed. Sub-section (6) to (7) deal with situation where, in a scheme of amalgamation, demerger, etc. as to how the provisions of sub-section (2), (3) and (4) of Section 35ABB would not apply but the provisions of this Section shall, as far as may be, apply to the amalgamated company or to the demerged company, apply to the resulting company as they would have applied to the amalgamating company if the latter had not transferred the licence or to the demerged company if the latter had not transferred the licence, as the case may be. Sub-section (8) states that where a deduction for any previous years under sub-section (1) is claimed and allowed in respect of any expenditure referred to in that sub-section, no deduction shall be allowed under the sub-section (1) of Section 32 for the same previous year or any subsequent previous year.

11.3. The salient aspects of Section 35ABB (1) of the Act may be read as under:

(i) ***Purpose and nature of expenditure -*** Capital expenditure incurred for the purpose of obtaining licence to operate telecommunication services.

(ii) ***Mode of amortisation of expenses -*** For each year of the relevant previous years, a deduction equal to the appropriate fraction of the amount of such expenditure, shall be allowed.

(iii) ***Conditions to be satisfied for applicability of the Provision –***

(a) The expenditure must be capital in nature;

(b) The expenditure must be incurred by an assessee for the purpose of acquisition of the right to operate telecom services;

(c) The said expenditure may be incurred before the commencement of business to operate telecommunication services, or thereafter at any time during any previous year;

(d) The expenditure must represent the payment actually made to obtain a licence.

12. Since the variable licence fee paid by the respondents-assessees to the DoT under the Telecom Policy of 1999 is stated to be imposed and collected on the strength of the Telegraph Act, the relevant provisions of the said Act are extracted hereinunder for immediate reference:

"4. Exclusive privilege in respect of telegraphs, and power to grant licences:-

(1) Within India, the Central Government shall have the exclusive privilege of establishing, maintaining and working telegraphs:

Provided that the Central Government may grant a licence, on such conditions and in consideration of such payments as it thinks fit, to any person to establish, maintain or work a telegraph within any part of India:

Provided further that the Central Government may, by rules made under this Act and published in the Official Gazette, permit, subject to such restrictions and conditions as it thinks fit, the establishment, maintenance and working-

(a) of wireless telegraphs on ships within Indian territorial waters and on aircraft within or above India, or Indian territorial waters, and

(b) of telegraphs other than wireless telegraphs within any part of India.

Explanation.-- The payments made for the grant of a licence under this subsection shall include such sum attributable to the Universal Service Obligation as may be determined by the Central Government after considering the recommendation made in this behalf by the Telecom Regulatory Authority of India established under sub-section (1) of section 3 of the Telecom Regulatory Authority of India Act, 1997 (24 of 1997).

(2) The Central Government may, by notification in the Official Gazette, delegate to the telegraph authority all or any of its powers under the first proviso to sub-section (1).

The exercise by the telegraph authority of any power so delegated shall be subject to such restrictions and conditions as the Central Government may, by the notification, think fit to impose."

(3) Any person who is granted a license under the first proviso to sub-section (1) to establish, maintain or work a telegraph within any part of India, shall identify any person to whom it provides its services by--

(a) authentication under the Aadhaar (Targeted Delivery of Financial and Other Subsidies, Benefits and Services) Act, 2016 (18 of 2016); or

(b) offline verification under the Aadhaar (Targeted Delivery of Financial and Other Subsidies, Benefits and Services) Act, 2016 (18 of 2016); or

(c) use of passport issued under section 4 of the PassportsAct, 1967 (15 of 1967); or

(d) use of any other officially valid document or modes of identification as may be notified by the Central Government in thisbehalf.

(4) If any person who is granted a license under the first proviso to sub-section (1) to establish, maintain or work a telegraph within any part of India is using authentication under clause (a) of sub-section (3) to identify any person to whom it provides its services, it shall make the other modes of identification under clauses (b) to (d) of sub-section (3) also available to such person.

(5) The use of modes of identification under sub-section (3) shall be a voluntary choice of the person who is sought to be identified and no person shall be denied any service for not having an Aadhaar number.

(6) If, for identification of a person, authentication under clause (a) of sub-section (3) is used, neither his core biometric information nor the Aadhaar number of the person shall be stored.

(7) Nothing contained in sub-sections (3), (4) and (5) shall prevent the Central Government from specifying further safeguards and conditions for compliance by any person who is granted a license under the first proviso to sub-section (1) in respect of identification of person to whom it provides its services.

Explanation.-- The expressions "Aadhaar number" and "core biometric information" shall have the same meanings as are respectively assigned to them in clauses (a) and (j) of section 2 of the Aadhaar (Targeted Delivery of Financial and Other Subsidies, Benefits and Services) Act, 2016 (18 of 2016).

xxx xxx

"8. Revocation of licences:- The Central Government may, at any time, revoke any licence granted under section 4, on the breach of any of the conditions therein contained, or in default of payment of any consideration payable there under."

xxx xxx

"PART IV

PENALTIES

20. Establishing, maintaining or working unauthorized telegraph:–

(1) If any person establishes, maintains or works a telegraph within India in contravention of the provisions of section 4 or otherwise than as permitted by rules made under that section, he shall be punished, if the telegraph is a wireless telegraph, with imprisonment which may extend to three years, or with fine, or with both, and in any other case, with a fine which may extend to one thousand rupees.

(2) Not withstanding anything contained in the Code of Criminal Procedure, 1898 (5 of 1898), offences under this section in respect of a wireless telegraph shall, for the purposes of the said Code, be bailable and non-cognizable.

(3) When any person is convicted of an offence punishable under this section, the Court before which he is convicted may direct that

the telegraph in respect of which the offence has been committed, or any part of such telegraph, be forfeited to Government."

"20A. Breach of condition of licence:– If the holder of a licence granted under section 4 contravenes any condition contained in his licence, he shall be punished with fine which may extend to one thousand rupees, and with a further fine which may extend to five hundred rupees for every week during which the breach of the condition continues."

"21. Using unauthorized telegraphs:– If any person, knowing or having reason to believe that a telegraph has been established or is maintained or worked; in contravention of this Act, transmits or receives any message by such telegraph, or performs any service incidental thereto, or delivers any message for transmission by such telegraph or accepts delivery of any message sent thereby, he shall be punished with fine which may extend to fifty rupees."

12.1. The Telegraph Act is the parent legislation under which licences to establish, maintain or work a telegraph are issued. Section 4(1) of the Telegraph Act states that the Central Government shall have the exclusive privilege of establishing, maintaining and working telegraphs. The proviso to Section 4(1) indicates that the Central Government may grant a licence to any person to establish, maintain or work a telegraph within any part of India on such conditions and in consideration of such payment as it thinks fit.

12.2. Section 8 of the Telegraph Act allows the Central Government to revoke at any time any licence granted under Section 4 thereof, on breach of any of the conditions therein contained or in default of payment of any consideration payable thereunder.

12.3. Section 20 of the Telegraph Act declares that any person who establishes, maintains or works a telegraph in contravention of the provisions of Section 4 shall be punished with imprisonment, which may extend to three years, or with fine, or with both. Section 20A and 21 deal with breach of conditions of licence and the consequences of using unauthorised telegraphs.

12.4. A bare perusal of the aforesaid provisions of the Telegraph Act would throw light onto the following aspects:

i. The Central Government may grant a licence to establish, maintain or work a telegraph, by granting a licence on payment of a licence fee, under the proviso to Section 4(1) of the Telegraph Act.

ii. The Central Government may, under Section 8, revoke any licence issued under Section 4 of the Telegraph Act, on ground of default in payment of consideration.

iii. Any contravention of Section 4 of the Telegraph Act, or of conditions of the licence issued under Section 4, would invite imprisonment and/or imposition of fine.

13. We shall now refer to the terms of the Licence Agreement entered into under the Policy of 1994 and the terms of migration of the existing licencees to the New Telecom Policy, 1999 regime, with a view to examine whether the nature and character of the licence fee was changed in light of migration.

13.1. For ready reference, a specimen licence agreement dated 29 November, 1994, in favour of Bharti Cellular Ltd. is extracted hereinunder. It is to be clarified at this juncture that the date of agreement with each respondents may be different but the terms are identical:

"Licence Agreement under the Indian Telegraph Act

This Agreement made the 29th day of November, 1994 between the President of India acting through the Director (TM-IX), Department of Telecommunications (called the Licenser) of the ONE PART and M/s. Bharti Cellular Ltd., registered under The Companies Act 1956 and having its registered office at 15th Floor, Devika Tower, 6 Nehru Place, New Delhi-110 019. (hereinafter called the Licensee which expression shall unless excluded by repugnant to this context be deemed to include its successor in business) of the OTHER PART.

Whereas in exercise of the powers of the Central Government under Sub Section 2 of Section 4 of the Indian Telegraph Act 1885, the Central Government delegated its powers to Telegraph Authority (hereinafter referred to as Authority) by GSR 806 Gazette of India, Part II, Section 3(i) dated 24th August 1985.

And whereas pursuant to the request of the Licensee the Authority has agreed to grant licence to the Licensee on the terms and conditions appearing hereinafter to establish, maintain and operate Cellular Mobile Telephone Service upto the subscriber's terminal connection (hereinafter called the Service) in the areas given in Schedule "A" annexed hereto and the Licensee has agreed to accept the same on the terms and conditions appearing hereinafter.

Now this Agreement witnesseth as follows:

1. In consideration of mutual covenants as well as the licence fee payable in advance in terms of schedule 'C' and observations and/ or due performance of all the terms and conditions to be observed/ performed on the part of the licensee, the Licenser does hereby grant licence to the Licensee to establish, maintain and operate Cellular Mobile Telephone Service upto the subscriber's terminal connection in the areas given in Schedule "A" annexed hereto on the terms and conditions mentioned in Schedule "C" annexed hereto.

2. The licence is granted initially for a period of 10 years extendible for one year or more at a time at the discretion of the authority, on such terms and conditions as the Authority may, at his sole discretion, agree provided that the Licensee is not in default or has committed/ any breach of any terms and conditions of the Licence. The licence fee payable is given in Schedule "C" condition 19 of this licence.

3. The licence is governed by the provisions of the Indian Telegraph Act, 1885 and Indian Wireless Telegraphy Act, 1933 as modified from time to time.

4. Unless otherwise mentioned in the subject or context appearing hereinafter the main body of the agreement and all the Schedules annexed hereto including the tender documents will form part and parcel of this agreement provided however in case of conflict terms of this agreement and those of schedules hereto will prevail over the tender documents.

5. In this Agreement words and expressions will have the same meaning as are respectively assigned to them in the Schedule "C" Part-I.

6. The licensee should clearly indicate the specifications of the service to the subscribers at the time of signing the contract with them.

7. The Ceiling Tariff to be charged from the subscribers of the service is given in Schedule "B" annexed hereto. Licensee can charge less tariff without any approval of the Authority.

8. The bank guarantees to be given by the licensee prior to the signing of the Licence Agreement is given in Schedule "D" annexed hereto.

9. The Licensee will not assign or transfer its rights in any manner whatsoever under the licence to a third party or enter into any agreement for sub-licence and/or partnership relating to any subject matter of the licence to any third party either in whole or in part i.e. no sub-leasing /partnership/third party interest shall be created.

10. In case of interruption of service lasting for more than 72 hours, an appropriate rebate shall be given to the users of the service by the Licensee. The Authority reserves the right to, in case of a default, impose any penalty as it may deem fit.

11. The Authority may at any time revoke the licence on the breach of any of the terms and conditions therein contained or in default of payment of any consideration payable thereunder by giving a 60 days notice.

12.1 The Licensee is not allowed to use any encryption in the network.

12.2 The Licensee is required to provide list of subscribers to the Authority every quarter regularly and, as and when required by the Authority.

12.3 The Authority or its representative will have an access to the MSC as well as the technical facility provided by the Licensee for monitoring, inspection etc. without giving any prior notice.

13. It is further agreed and declared by the parties that notwithstanding anything contained hereinbefore, that

(i) The licence is issued on non-exclusive basis. The Authority reserves the right to operate the service within the same geographical area.

(ii) The Authority reserves the right to modify at any time the terms and conditions of the licence covered under Schedules "A", "B", "C", and "D", annexed hereto, if in the opinion of the Authority it is necessary or expedient to do so in the interests of the general public or for the proper conduct of telegraphs or on security consideration.

(iii) The Authority reserves the right to revoke the licence at any time in the interest of public by giving a 60 days' notice.

(iv) Notwithstanding anything contained anywhere else in the licence the Authority's decision shall be final.

(v) The authority reserves the right to take over the entire services and networks of the licensee or revoke/ terminate /suspend the licence in the interest of national security or in the event of a national emergency/ war or low intensity conflict type of situations.

In Witness whereof the parties hereto have caused this Agreement to be executed through their respective authorized representatives the day and year first before written

Signed and Delivered

for and on behalf of

President of India"

(*Emphasis by us*)

13.2. The conditions on which the licence was granted were stipulated in Schedule A and Schedule B of the licence agreement. The payment of licence fee was in the following terms:

"PAYMENT OF LICENCE FEES

19.1 The Licence fee payable by licencee for each service area shall be regulated as follows: -

Licence Fee For

Service Area	1st Year	2nd Year	3rd Year
	(Rupees in Crores)		
Bombay	3	6	12

Delhi	2	4	8
Calcutta	1.5	3	6
Madras	1	2	4

4th Year and onwards

@ Rs. 5 lakhs (five lakhs) per 100 (one hundred) subscribers or part thereof; subject to the minimum shown below :-

Minimum Licence Fee for

Fourth to Sixth Service Area	Year Seventh (for each year)	year) year onwards (for each year) (Rs.in crores)
Bombay	18	24
Delhi	12	16
Calcutta	9	12
Madras	6	8

a) For purpose of charging the lump-sum Licence fee for the first three years, the year shall be reckoned as twelve months, beginning with the date of commissioning of services or completion of 12 months from date of signing of Licence Agreement, whichever is earlier.

b) The fourth year for purpose of charging the Licence fee shall be the period from the completion of the third year as defined above to the 31st day of March succeeding. The annual Licence Fee for the fourth year will therefore, be computed prorate with reference to the actual number of days. Thereafter, the year for purpose of levy of Licence fee shall be the financial year i.e. 1st April to 31st March and part of the year as balance period, if any.

c) For the purpose of calculation of Licence fee from the fourth year onwards as indicated in para 19.1 above, the number of subscribers at the end of each month shall be added for all the months of the year and divided by the number of completed months.

XXX

(f) The rate of Rs. five lakhs per hundred subscribers or part thereof is based on the unit call rate of Rs. 1.10. Fourth year onwards, as defined in the clause 19.1(d), the rate of Rs. five lakhs will be revised based on the prevalent unit call rate. The revision will be limited to 75% of the overall increase in the unit rate during the period preceding such revision."

The Agreement further stipulated:

"19.2 On completion of three years from the date of commissioning/ provision of services; the Authority reserves the right to fix the share of the gross revenue from rental, air time charges for all other services provided from the cellular network of the Licensee, as additional licence fee.

19.3 The annual Licence fee as prescribed above does not include Licence fees payable to WPC wing of Ministry of Communications (WPC) for use of Radio Frequencies which shall be paid separately by the Licensee on the rates prescribed by the WPC and as per procedure specified by it (condition 20)."

13.3. The key features of the licence agreement under the 1994 Policy regime may be enumerated as under:

i. The licence was granted enabling the licencee to establish, maintain and operate cellular mobile telephone service, within a given geographical area.

ii. The licence was granted for a period of ten years, which was extendable for five years or more, at the discretion of the licensor, i.e., the Central Government, unless terminated earlier.

iii. Fixed amount of licence fee was to be paid for the first three years, irrespective of the number of subscribers, as provided in paragraph 19 of the agreement and such amounts was subject to increase annually.

iv. From the fourth year onwards, the amount of licence fees to be paid, was dependent on the number of subscribers, irrespective of the revenue accrued by the licencee from such subscribers, subject to the prescribed minimum.

v. The consequence of non-payment of licence fee was termination of the licence agreement.

vi. In accordance with the Policy of 1994, the condition of maintaining duopoly in the market was formalised in the licence agreement.

vii. The licence was non-assignable.

13.4. Subsequently, with a view to implement the Policy of 1999, letters dated 27 July, 1999 were issued by the DoT proposing the package for migration of existing licencees to the Policy of 1999 regime. It was stated that the conditions prescribed therein are to be accepted as a package, in entirety. Pursuant to the acceptance of the terms of migration, the original licence agreement was amended. The relevant portions of a specimen letter evidencing the amendments is extracted as under:

"GOVERNMENT OF INDIA

MINISTRY OF COMMUNICATIONS

DEPARTMENT OF TELECOMMUNICATIONS

(VAS CELL)

SANCHAR BHAWAN,

20, ASHOKA ROAD,

NEW DELHI-110001

No 842-47/2000-VAS/Vol. IV

Dated: January 29, 2001

To

M/s Bharti Cellular Ltd.

D-184, OKHLA Industrial Area, Phase-1,

New Delhi-110 020.

Subject:- Amendment in the Licence Agreement No 842-1893-TM Dated 29.11.1994 for Cellular Mobile Telephone Service in Delhi

Metro Service Area as a consequence to Migration to revenue sharing regime of New Telecom Policy-1999 (NTP-99)

Sirs,

In consideration of the acceptance by the Licensee, of the terms and conditions contained in the offered Migration Package vide No. 842-153/99-VAS (Vol. V) (Pt.) dated 22.7.1999 for migration to the revenue sharing regime under New Telecom Policy-1999, the license agreement shall stand substituted and modified as follows with effect from 1.8,1999, notwithstanding anything contained in the License Agreement:

(i) The Licensee shall forego the right of operating in the regime of limited number of operators after 01.08.1999 and shall operate in a multipoly regime, that is to say that the Licensor may issue additional licenses for the Service without any limit in the Service Area where the Licensee Company is providing Cellular Mobile Telephone Service.

(ii) Licence fee: With effect from 1.8.1999, the payable license fee shall be equal to prescribed percentage as share of gross revenue of the Licensee Company. Provisionally the licensor has fixed 15% of the gross revenue as license fee and presently the gross revenue for this purpose shall mean the total revenue of the Licensee Company under the license excluding,

(a) the PSTN related call charges paid to Bharat Sanchar Nigam Limited (BSNL)/MTNL or any other Telecom Service Provider and,

(b) service tax or charge collected by the Licensee on behalf of the Government from their subscribers.

The Government will take a final decision about the quantum of revenue share, definition of revenue for this purpose, after taking into consideration the recommendations of

(iii) Period of Licence: The period of license shall be twenty years from the effective date of the existing license agreement unless terminated for the reasons stated therein. The Licensor may extend the period of license, if requested during 19th year from the effective date for a period of 10 years at a time on mutually agreed terms and conditions The decision of licensor shall be final in regard to grant of extension.

(iv) The acceptance of the Migration Package shall be taken and deemed as full and final settlement of all existing disputes whatsoever, for the period upto 31.7.1999 (the cut-off date) irrespective of whether they are related to the Migration Package or not. No dispute or difference shall be raised by the licensee for the said period at any later date."

(*Emphasis supplied*)

13.5. Thereafter, the DoT introduced further amendments to the licence agreement, w.e.f. 01 August, 1999. The relevant portions of a specimen letter dated 25 September, 2001 evidencing the amendments is extracted as under:

"GOVERNMENT OF INDIA

MINISTRY OF COMMUNICATIONS

DEPARTMENT OF TELECOMMUNICATIONS

(VAS CELL)

SANCHAR BHAWAN,

20, ASHOKA ROAD,

NEW DELHI-110 001

Dated 25 September, 2001

No.842-47/2000-VAS(Vol. IV) (Part)

To

M/s Bharti Cellular Ltd.

D-184, Okhla Industrial Area,

Phase-1, New Delhi-110020.

Subject: Amendment in the Licence Agreement No. 842-18/93-TM dated 29.11.1994 for Cellular Mobile Telephone Service in Delhi

Service Area as a consequence to Migration to revenue sharing regime of New Telecom Policy-1999 (NTP-99).

In continuation of Amendment dated 29th January, 2001 of the aforesaid License Agreement and more specifically Para (ii) thereto, reserving the power to take a final decision on the quantum of license fee and WPC charges; the licensor hereby decides the following in pursuance of the said power which shall modify and supersede whatever is contained and described in the Licence Agreement or the above stated Amendment.

(i) Annual License fee at the rate of 15% of Adjusted Gross Revenue (AGR) shall be payable by you, with effect from 1st August, 1999.

(ii) In addition the cellular licenses shall pay spectrum charges, with effect from (1.8.1999) the cut-off date of change over to NTP-99 regime, on revenue share basis of 2% of AGR towards WPC Charges covering royalty payment of the use of cellular spectrum upto 4.4 MHz+4.4 MHz and Licence fee for Cellular Mobile handsets & Cellular Mobile Base Stations and also for possession of wireless telegraphy equipment as per the details prescribed by Wireless Planning & Coordination Wing (WPC). Any additional band width, if allotted subject to availability and justification shall attract additional License fee as revenue share (typically) 1% additional revenue share if Bandwidth allocated is upto 6.2 MHz + 6.2 MHz is place of 4.4 MHz+4,4 MHz)."

(*Emphasis supplied*)

13.6. The pertinent qualitative changes effected in the licence conditions, following migration into the Policy of 1999 regime, may be presented in a tabular form, as under:

Sl. No.	***Parameters for Distinction***	***National Telecom Policy, 1994***	***New Telecom Policy, 1999***
1.	Details of the payment to be made by the operator:	i. Fixed licence fee for the first three years; ii. From the fourth year onwards, the amount of licence fees to be paid, was dependent on the number of subscribers, irrespective of the revenue account by the licencee from such subscribers, subject to the prescribed minimum	i. One-time entry fee paid by existing telecom operators and entry fee that was paid by all the new entrants; ii. Variable annual licence fee paid as a percentage of AGR.
2.	Maximum number of operators permissible in a circle	Two	No restriction
3.	Validity of the licence	10 years, subject to extension.	20 years, subject to extension.
4.	Right of the operator/ licencee to assign/ transfer the licence	Licence was non-assignable and non-transferable.	Restriction on assignment/ transfer of licence was relaxed.

14. The discussion on the points set out above, in our view, must begin with a detailed review of relevant case law detailing the nature and

characteristics of capital expenditure and revenue expenditure and the tests to identify the same.

14.1. In the impugned order, the High Court of Delhi found that there was no decision of the Supreme Court or any of the High Courts directly applicable to the factual matrix of the case and therefore, considered a number of decisions of this Court which we shall refer to as under:

(a) At the outset, we preface our discussion by the observations of this Court in ***Alembic Chemical Works Co. Ltd. vs. CIT, (1989) 3 SCC 329 ("Alembic Chemical Works Co. Ltd.")*** wherein the transaction in question was with regard to the one-time payment made under an agreement with a foreign firm, by the assessee, to obtain technical know-how for increasing yield of penicillin in its existing plant. While considering the nature of the said transaction, this Court indicated that *"in the infinite variety of situational diversities in which the concept of what is capital expenditure and what is revenue arises,"* it is not possible *"to formulate any general rule even in the generality of cases, sufficiently accurate and reasonably comprehensive, to draw any clear line of demarcation"*. This Court further held that there is no single definitive criterion which by itself demarcates whether a particular outlay is capital or revenue. Therefore, the "once for all" test as well as the test of "enduring benefit" may not be conclusive. Consequently, the various terms and conditions of the agreement, the advantages derived by an assessee under the agreement, the payment made by the assessee under the agreement are all to be taken into account and then it has to be decided whether the whole or a part of the payment thus made is a capital expenditure or a revenue expenditure.

This Court observed that courts have applied different tests like starting of a new business on the basis of technical know-how received from the foreign firm; exclusive right of the company to use the patent or trademark which it receives from the foreign firm; the payments made by the company to the foreign firm whether, a definite one or dependent upon certain contingencies; right to use the technical know-how for production even after the completion of the agreement; obtaining enduring benefit for a considerable part on account of the technical information received from a foreign firm, payment whether made "once for all" or in different installments co-relatable to the percentage of gross turnover of the product, etc. to ultimately find out whether the expenditure or payment thus made makes an accretion to the capital asset(s) and after the court comes to the conclusion that it does, then, has to be held to be a capital expenditure.

It was further observed that no single definitive criterion by itself would be determinative and therefore, bearing in mind the changing economic realities of business and the varieties of situational diversities, the various clauses of the agreement are to be examined.

On fact, as regards the question as to whether "once for all" payment made under an agreement with a foreign firm by the assessee to obtain technical knowhow, for increasing yield of penicillin in its existing plant with a condition to keep the said know-how confidential, constituted business expenditure allowable for deduction, this Court held in the affirmative. M.N. Venkatachalia, J. (as the learned Chief Justice then was) held that in computing the income chargeable under the head "Profits and Gains of Business or Profession", Section 37 of the Act enables the deduction of any expenditure laid out or expended wholly and exclusively for the purpose of the business or profession, as the case may be. The fact that an item of expenditure is wholly and exclusively laid out for purposes of the business, by itself, is not sufficient to entitle its allowance in computing the income chargeable to tax. In addition, the expenditure should not be in the nature of a capital expenditure.

(b) In ***Empire Jute Co. Ltd.,*** the question which arose was whether the sale of loom hours was to be held to be in the nature of capital receipt and hence not taxable. he transaction involved one jute mill transferring loom hours to another for consideration, subject to certain conditions. It was observed in the said case that a capital expenditure would be for securing an enduring benefit but when it comes to acquiring an advantage in the commercial sense, the enduring benefit test should not be applied mechanically. In the said case, another test was adopted, i.e., fixed and circulating capital test. It was observed that the purchase of loom hours was not like circulating capital (labour, raw material, power etc.) but loom hours were also not part of fixed capital. It was observed that whether an expenditure is revenue or capital should depend upon practical and business considerations rather than juristic classification of legal rights. That the test to be adopted was whether the expenditure was in view of a business necessity or expediency, i.e., was the expenditure a part of assessee's working expenditure or a part of process of profit earning; whether the expenditure was necessary to acquire a right of permanent character, the possession of which was a condition for carrying on trade was highlighted.

(c) Insofar as lease agreements are concerned, this Court in ***Assam Bengal Cement Co. Ltd.,*** in the context of acquiring lease of mining stone quarries for manufacture of cement for twenty years on payment of yearly rent as well as protection fee to ward off competition held the same to be capital expenditure. It was observed in the said case that the consideration payable was per annum but was for the entire or whole duration of the lease and it protected and gave right to the assessee to carry on business unfettered from outsiders. It was held that the expenditure was not a part of the working or operational expenses but for acquiring a capital asset.

(d) In ***Sindhurani,*** salami or lump-sum payment of non-recurring nature made by the prospective tenant to the landlord as consideration for settlement of agricultural land and parting with certain rights paid anterior to landlord and tenant relationship was held not to be in the nature of rent and thus capital payment. It was held that the payment was not for use of land but for the land to be put to use by the assessee. Salami was not rent paid in advance.

(e) In ***Enterprising Enterprises,*** this Court affirmed the decision of Madras High Court after referring to ***Pingle Industries Ltd. vs. CIT, (1960) 40 ITR 67 (SC) ("Pingle Industries Ltd."); Gotan Lime vs. CIT, (1999) 239 ITR 718 ("Gotan Lime")*** and ***Aditya Minerals Pvt. Ltd.*** to hold that there is a distinction between a payment of royalty or rent and where the entire amount of lease premium was paid either at one time or in instalments. Royalty or rent is a revenue expenditure whereas the payment of a lease premium either at one time or in instalments would be a capital expenditure.

14.2. Having referred to the aforesaid decisions, three other judgments were noticed by the Delhi High Court which, according to learned ASG appearing for the appellant-Revenue were erroneously applied to the case at hand. They could be alluded to as under:

(a) In ***Jonas Woodhead and Sons,*** the question was whether 25% of the gross revenue paid as royalty to the foreign company for technical information/know-how relating to setting up of a plant for manufacture of products, was capital expenditure. The issue depended upon several factors including whether the assessee had set up an entirely new business, or whether the technical knowhow was for the betterment of the product which was already being produced; whether it was a part and parcel of the existing business or a new business?; whether on expiry of the period of agreement, the assessee was required to give back the plans, drawings etc., which were obtained from the foreign company or could continue to manufacture the products? The assessing officer in the said case had treated 25% of the amount paid as royalty as capital and the balance amount was treated as revenue expenditure.

The question that came up for consideration before this Court was, whether, on the facts and in the circumstances of the said case, the Tribunal was right in holding that 25% of the amount paid by the assessees therein as royalty to Jonas Woodhead and Sons was capital expenditure and therefore not allowable as revenue expenditure under the provisions of the Act for the Assessment years 1961-1968 and 1968-1969.

It was observed that this question would depend upon several factors stated above and the cumulative effect of a construction of the various terms and conditions of the agreement; whether the assessee derived benefits coming to its capital for which the payment was made or not so.

Considering the different clauses of the agreement in the said case, it was concluded that the agreement with the foreign firm was to set up a new business by the assessee and the foreign firm had not only furnished information and technical know-how but had also rendered valuable services in setting up of the factory itself and even after the expiry of the agreement, there was no embargo on the assessee to continue to manufacture the product in question. Therefore, it was difficult to hold that the entire payment made was a revenue expenditure merely because the payment was required to be made on a certain percentage of the rates of the gross turnover of the products of the income as royalty. That alone did not make it a revenue expenditure. Therefore, the question raised was answered in favour of the Revenue and the appeals filed were dismissed.

b) In ***Southern Switch Gear Ltd.,*** this Court affirmed the decision of the Madras High Court, wherein royalty payable was apportioned and 25%

thereof was treated as capital payment or expenditure on the ground that the right to manufacture certain goods exclusively in India should be taken as an independent right secured by the assessee from the foreign company and this right was of enduring nature.

(c) In ***Best and Co.,*** the respondent assessee therein was carrying on business and had innumerable agencies and compensation was received on account of cancellation of one agency and the question was, whether, the said compensation was capital or revenue receipt in nature; whether by the termination of an agency the asseessee therein had lost an earning asset and the compensation paid for the destruction of such an asset was a capital receipt and therefore not liable to tax. K. Subba Rao. J. (as the learned Chief Justice then was) speaking for a three-Judge Bench observed that the question, as to, whether, the compensation received by an assessee for the loss of agency is a capital receipt or a revenue receipt depends upon the circumstances of each case. This is because many questions have to be asked and answered, particularly, whether the loss of an agency was an ordinary incidence in the course of business or did it amount to loss of an enduring asset causing an unabsorbed shock dislocating the entire or a part of the earning apparatus or structure. It was held that if a loss of a particular agency was incidental to the business, compensation received would be a revenue receipt but if it was compensation received for the loss of an enduring asset, then it would be a capital receipt. But for this, the previous history of the business and relative importance of the agency lost and the position of the business after the loss of the said agency have to be scrutinized by the department. While considering the said issue, on the facts of the said case, it was held that the asseessee therein was a well-established and long standing company in South India which had taken up innumerable agencies in different lines and one such agency had been taken from the Imperial Chemical Industries (Exports) Limited, Glasgow. When there was no material to show that the loss of the said agency was so large that the business of the agency was dislocated, on considering the facts of the said case, this Court observed that the loss of the said agency by the assessee was only a normal trading loss and the income it received was revenue receipt.

Another question which was considered was whether compensation received by the assessee in lieu of a restrictive covenant was a capital receipt. It was observed that the non-compete clause came into operation after the termination of the agency and it was an independent obligation undertaken by the assessee therein not to compete with the new agent in the same field for a specified period and therefore, the compensation received was attributable to the restrictive covenant and was a capital receipt and hence not assessable to tax.

The majority judgment answered the said question by observing that compensation on cancellation of an agency could be both capital and revenue depending upon facts of each case and whether, the cancellation had affected the earning apparatus or structure from a physical, financial, commercial and administrative point of view. In the said case, compensation received was held to be revenue receipt as the respondent assessee had innumerable agencies in different lines and had given up only one to continue business in other lines. Loss of an agency, it was observed, was in the normal course of business and a part of normal business, therefore, the amount received as compensation was revenue in nature. At the same time, it was accepted that the compensation paid/received on account of a restrictive covenant for a specified period on which the assessee had undertaken not to take up competitive agency was a capital receipt and therefore, not taxable.

14.3. In ***Alembic Chemical Works Co. Ltd.,*** on facts, it was observed that the improvisation in the process and technology in some areas of the enterprise was supplemental to the existing business and there was no material to hold that it amounted to a new or fresh venture. That the further circumstance that the agreement pertained to a product already in the line of the established business of the assessees and not to a new product indicated that what was stipulated was an improvement in the operations of the existing business and its efficiency and profitability not removed from the area of the day-to-day business of the assessee.

In the above context, it was held that the expenditure was in the nature of a revenue expenditure and not capital expenditure. It was further observed that there was no material before the Tribunal to hold that the area of improvisation was not a part of the existing business or that the entire existing manufacturing operations for the commercial production of penicillin in the assessees existing plant had become obsolete or inappropriate in relation to the exploitation of the new sub-cultures of the high-yielding strains of penicillin supplied by a company, Meiji and that the mere introduction of the new bio-synthetic source required the erection and commissioning of a totally new and different type of plant and machinery.

14.4. Another case which has been discussed by the High Court in the impugned Judgment and relied upon by the appellant–Revenue is ***Pingle Industries Ltd.*** In the said case, the majority judgment stated that the payment in question therein was made with a view to acquire a long-term lease and a right to mine stones and the lease was conveyed to the assessee who had to extract the stones and convert them as a stock-in-trade. That the expenditure was incurred towards securing a capital asset from which, after extraction, stones could be converted into stock-in-trade. The payment, though periodic, in fact, was neither rent nor royalty but a lump-sum payment in instalments for acquiring a capital asset of enduring benefit to his trade. In this view of the matter, the High Court treated the outgoings as on capital account. On facts, it was observed that the assessee therein had made a down payment of Rs.96,000/- and for the remaining amount for the acquisition of lease had asked for easy terms. The remaining amount was paid every month but it was not for acquisition of the right from month to month. According to this Court "it was really the entire sum chopped into small payments for his convenience." Hence, the amount could not be described as a business expense, because the outgoings every month were not to be taken as spent over purchase of stones but in discharge of the entire liability to the jagir. This was because the lease was taken to excavate stones from certain quarries in six villages from the quarry situated therein.

The assessee had undertaken not to manufacture cement and not to allow any other person to excavate stones in the area of those six villages. The lease was in the nature of exclusive right and a monopoly. In case of any default of the instalment, the contract would be re-auctioned after one month's notice to the contractor, who would be responsible for any shortfall but would not have the benefit of any extra amount.

14.5. Learned ASG also relied upon the judgment in Jalan Trading Co. In the said case, a manufacturing company gave its sole selling agency to a firm, namely, Jalan Trading Company for two years with a right to renew by an agreement under a deed of assignment. The benefit of the agreement was assigned to the assessee on its payment of 75% of its profit and commission, remuneration and other moneys received under the said agreement or any further agreement. The assessees therein claimed the payment of 75% of their profits in the relevant assessment year as a business deduction. The question was, whether, the payment was a revenue expenditure or a capital expenditure. It was observed, on facts, that the assessee therein was a new company and it had acquired under the contract the right to carry out a business on a long-term basis subject to the renewal of the agreement on payment of 75% of its annual net profits. The question was whether the assessee had acquired a capital asset and therefore, the payment was not admissible as a deduction under Section 10(2)(vii) of the Act. On perusing the clauses of the deed of assignment, this Court held that the payment of 75% of the profits and commission paid under the said agreement was in the nature of a capital expenditure and the same was not allowable as a deduction under the Act.

14.6. Learned senior counsel Sri Datar relied upon four decisions which we shall discuss as under:

(a) In Travancore Sugars and Chemicals Ltd. vs. Commissioner of Income-tax, (1966) 62 ITR 566 (SC) ("Travancore Sugars and Chemicals Ltd."), the facts were that three undertakings run by the Government of Travancore were taken over by a company under an agreement wherein the assets of the three undertakings were agreed to be sold by the Government to the new company. Cash consideration for the sale of the assets of the three undertakings was to be paid and also 20% of the annual net profit subject to a maximum of Rs.40,000/- was to be paid to the Government. The said 20% was later reduced to 10% by an amendment of the terms of the agreement. The question was, whether, the said payment was allowable under Section 10 of the Act. The High Court held that the amount constituted a capital expenditure. However, this Court held that the payment in question was in the nature of revenue expenditure for the following reasons:

i) The payment was for an indefinite period and had no limitation of time attached to it.

ii) The payment was related to the annual profits which flowed from the trading activities of the appellant-company and had no relation to the capital value of the assets and;

iii) The payment was not related to or tied up, in any way, to any fixed sum agreed between the parties as part of the purchase price of the three undertakings.

This Court held that the real nature of the transaction had to be gathered not only from concerned documents but also from the surrounding circumstances.

(b) In ***M/s. Devidas Vithaldas and Co. vs. C.I.T., Bombay City, (1972) 3 SCC 457, (1972) 184 ITR 277 (SC) ("Devidas Vithaldas and Co.")*** this Court was dealing with the question regarding acquisition of a running business and whether, the acquisition of goodwill of the business would amount to an acquisition of a capital asset and the purchase price will be a capital expenditure. This Court also considered the question whether, it would make any difference whether, the consideration is paid in lump-sum, or at one time, or in instalments, distributed over a definite period. It was held that where the acquisition is not of the goodwill itself but for the right to use it, the expenditure would be a revenue expenditure. It was further observed that if the payment is in the nature of royalty it has to be treated as a revenue expenditure. The main reason for holding that the transaction did not amount to the sale of goodwill was that the duration of the payment as also the amount of consideration was indefinite as they depended on the rise and fall in the profits of the business. In the said case, it was observed by a majority of 3:1 that *"in distinguishing between capital and revenue expenditure, the courts have applied in different cases different tests. Nonetheless, it is recognised that none of them by itself is conclusive and the determination one way or the other has to be made on the facts and circumstances of each case.*

However, Sikri, C.J. in his dissenting opinion reasoned that the mode of payment of purchase price of any capital asset cannot convert the capital payment into a revenue payment in the hands of the vendee. The mode of payment may affect the character of the receipt in the hands of the vendor but as far as the vendee is concerned, what is obviously a capital payment cannot be converted to a revenue payment. However, the majority held that the transaction did not amount to a sale and that the payment of consideration for the use of the goodwill of the business which is indefinite and depends on the profits earned by the company each year can be a revenue expenditure.

(c) Reliance was also placed on ***Sarada Binding works*** by Sri Datar. In the said case, a registered firm carrying on business as a book binder and publisher had entered into an agreement with "B" under which it obtained the right to run the business of a publication concern for a consideration of a fixed sum of Rs.5,000/- per annum plus a sum equivalent to 10% of the net profits of each year of business. The assessee claimed the said amount as a business expenditure. The Madras High Court held that where the transaction in question amounted to a purchase of the business, the consideration paid partly as a fixed annual sum and partly a periodical payment on a certain percentage of the profits earned by the assessee from the said business could not be treated entirely as capital payment. The fixed annual sum payable was a capital payment but the periodical payments of sums which were indefinite depending upon the future profits earned could not be treated as capital in nature. In the said case, the following extract from Wheatcroft's treatise on The Law of Income Tax, Sur Tax and Profits Tax, was quoted wherein three types of cases where the purchase price may be paid periodically or in instalments and the points of distinction between them were quoted:

"First, there are cases where all the payments must be treated as income of the recipient and the payer is entitled to deduct tax on payment and to a deduction in computing his total income. Secondly, there are cases where the payments are all treated as capital and are neither taxable to the recipient nor deductible in computing the payer's total income. Thirdly, there are cases where the payments must be dissected into an income content and a capital content so that the former part is taxable and deductible whilst the latter is not."

On facts, the case before was classified as falling under the third category and it was held that the question, whether, the payment is capital or revenue has to be considered in relation to the facts of each case and the true nature of the payment has to be ascertained from the documents and all the surrounding circumstances with the important features to consider being the nature of the original obligation, the period of time during which the payments are to continue, whether or not they are expressed in the form of instalments of some capital sum and what provisions, if any, are made for commutation.

Further, four tests in deciding the question, whether, a particular expenditure is allowable or not were also quoted from the same treatise. The said extract is as under:

"In general, however, in order to decide whether some particular expenditure of a trader should be brought into account, four tests, similar to those considered in relation to receipts, should be applied. First, is the expenditure wholly and exclusively laid out for the purposes of the trade? If not, it will be excluded. Secondly, is the expenditure of a revenue, and not of a capital nature ? Unless it is of a revenue nature it will be excluded. Thirdly, may tax be deducted and retained on payment ? If so, it will be excluded. Finally, is there some other special provision of the Income-tax Act which permits, or requires, the payment to be brought in, or left out of account ?"

Therefore, in the said case, the Madras High Court held that the payments were of revenue character and that there were no elements present which would justify the court in attributing to the payments a capital character. The payments were fixed with reference to the profits which were indirectly related to the turnover. The payments were not related to any specified sum which was agreed upon by the parties as purchase price of the business. The decision of the Madras High Court was upheld by this Court.

(d) Sri Datar has also referred to the decision of this Court in ***Mewar Sugar Mills Ltd.*** In the said case, a licence was granted by the then ruler of Udaipur State for the manufacture of sugar which was to be a monopoly enduring to the assessee's benefit for thirty two years. One of the conditions was that no permission would be granted to any other person for starting a sugar factory for a period of thirty-two years from the date of the said order. Another condition was that royalty must be charged on the sugar manufactured in the factory. No other tax was to be charged. After the grant of the monopoly, a limited company was floated called the Mewar Industries Ltd. and the company took steps to set up a factory, obtained requisite machinery and installed it. After completion of the factory, production could not be started on account of financial difficulties. As a result, an agreement was entered into with two other persons to acquire from the company all the rights and assets held by it for the unexpired period of twenty-eight years and to run the business in consideration of the payment of 10% of the net profits. Before this Court, two controversies arose, namely, i) relating to the deduction of the payments made by the appellant therein for monopoly rights and ii) concerning the payment to the State of the royalty of the price of sugar manufactured by the company. The challenge to the question as to the disallowance of the payments made by the assessee in respect of the monopoly rights was given up. The only other question being that the payment of 2% royalty on the price of sugar manufactured by the appellant therein was relatable to the monopoly rights and therefore was capital expenditure was considered.

It was found that the payment of the 2% royalty on the price of sugar manufactured by the appellant therein had no relationship with the payment referable to the monopoly conferred under the grant. It was observed that on the facts and circumstances of the said case, the expenditure incurred, that is, payment of 2% royalty payment on the sugar manufactured was a revenue expenditure while the payment made in respect of the monopoly rights obtained was of a capital nature.

The applicability of the judgments discussed hereinabove to the case at hand, shall be examined at a later juncture.

15. A tabular representation outlining the classification of different transactions by this Court in various cases, is as under:

Sl. No.	***Citation***	***Transaction In Question***	***Classification of the Transaction in Question by this Court:***	***Reasons for classification:***
1.	***Assam Bengal Cement Co. Ltd. vs. Commissioner of Income Tax, West Bengal, (1955) 27 ITR 34 (SC).*** ***West Bengal, (1955) 217 ITR 34 (SC).***	Payment made by the assessee for acquiring a lease of mine stone quarries for the manufacture of cement, for a period of twenty years, on payment of yearly rent as well as a protection fee to ward off competition.	**Capital expenditure**	It was held that the expenditure was not a part of working or operational expenses, but was for acquiring a capital asset. The expenditure was held to be a capital expenditure although it was payable per annum, as it protected and gave the right to the assessee to carry on business unfettered by outsiders.
2.	***Member of the Board of Agricultural Income Tax, Assam vs. Sindhurani Chaudurani, (1957) 32 ITR 169 (SC).***	Lump-sum payment (non-recurring) made by the prospective tenant to the landlord as consideration for settlement of agricultural land.	**Capital expenditure**	It was held that such payment was not in the nature of rent, but in the nature of capital expenditure as the same was incurred prior to the coming into effect of the landlord-tenant relationship.

3.	***Pingle Industries Ltd. vs. Commissioner of Income Tax, (1960) 40 ITR 67 (SC).***	Lump-sum amount, payable in instalments for acquiring exclusive monopoly rights to extract flag stones from certain quarries.	**Capital expenditure**	That the assessee had acquired through the long term lease, the right to extract stones and that the lease conveyed to the assessee a part of the land. The lease was held to be a capital asset, which could be converted into stock-in-trade.
4.	***Commissioner of Income Tax, U.P. vs Maheshwari Devi Jute Mills Ltd., (1965) 57 ITR 36 (SC).***	Receipt of the assessee on sale of loom-hours.	**Capital receipt**	That the surplus loom-hours were disposed of by the assessee and no interest remained therein with the assessee. It was not a case of exploitation of the loom hours by permitting an additional user, while retaining ownership. Therefore, receipt by sale of loom hours must be regarded as a capital receipt.
5.	***R.B. Seth Moolchand Suganchand vs. Commissioner of Income Tax, Delhi, (1973) 3 SCC 257.***	Prospecting licence fee and tender money for mica mining rights for a period of twenty years.	**Capital expenditure**	That 1/20th of the licence fee could not be claimed as revenue expenditure on a yearly basis. That the lease in question was for a long period; the amount paid was for acquiring a right of enduring nature to extract and remove the Mica and bring it to the surface.

6.	***CIT, Bombay vs. Jalan Trading Co., (1985) 4 SCC 59.***	75% profit share, paid as consideration under a deed of assignment, for the right to carry on business.	**Capital expenditure**	That what was conveyed was the right to carry on the whole business and what was agreed to be paid was a profit share of 75% every year, as consideration to acquire this right. The fact that the payments were made annually would have no bearing on the nature of the transaction.
7.	***Commissioner of Income Tax vs. Bombay Burmah Trading Corporation, (1986) 161 ITR 386 (SC).***	Lump-sum consideration paid by the assessee for surrender of export rights in a forest lease, where the assessee had the right to extract and cut timber and remove them on payment of royalty.	**Capital expenditure**	That the payment was for sterilisation of the profit-making apparatus, i.e., the capital asset. The payment was not only with a view to earn profit in a new form, but was made to structure the assessee's profit-making apparatus and affected the conduct of business.
8.	***Aditya Minerals Pvt. Ltd. vs. Commissioner of Income Tax, (1999) 239 ITR 817.***	Advance rent for fifteen years to be paid, calculated at the rate of Rs. 35/- per month, for lease of land for excavation of minerals and subsidiary purposes.	**Capital expenditure**	That the rent paid by the assessee was in the nature of a deposit and was adjustable against the rent of each month. Since the rent for the entire period of lease was paid in advance, the expenditure would be capital expenditure. Reliance was placed on Pingle Industries Ltd.

9.	***Enterprising Enterprises vs. Deputy Commissioner of Income Tax, (2007) 293 ITR 437 (SC).***	Proportionate lease rent paid by mining lessee for acquiring leasehold right for extracting minerals from mineral bearing land.	**Capital expenditure**	Acquisition of a leasehold right to extract minerals.
10.	***M/s Gotan Lime Syndicate vs. Commissioner of Income Tax, (1966) 59 ITR 718 (SC).***	Royalty paid by the assessee per annum in lieu of a mining lease/ rights to excavate limestone in a certain area.	**Revenue expenditure**	That the lease was for excavation of limestone alone and no other rights were created in immovable property. That the royalty paid was not a payment for securing enduring advantage but was a payment in order to obtain raw material and hence, was in the nature of a revenue expenditure.
11.	**Commissioner of Income Tax vs. Best and Co. (Pvt.) Ltd. (1966) 60 ITR 11 (SC).**	Compensation received by the assessee on account of cancellation of one of its agencies.	**Revenue receipt**	That the assessee had innumerable agencies in different lines and had given up only one, to continue business in other lines. Loss of agency was in the normal course of business and a part of normal business, therefore, the amount received as compensation was revenue in nature.

12.	***Travancore Sugars and Chemicals Ltd. vs. Commissioner of Income-tax, (1966) 62 ITR 566 (SC).***	Payment of 20% of the annual net profits subject to a maximum of Rs.40,000/- which was to be paid to the Government by the assessee, in addition to a one-time cash consideration, on taking over three undertakings run by the Government of Travancore.	**Revenue expenditure**	That the payment was to be made for an indefinite period and had no limitation of time attached to it; The payment was related to the annual profits which flowed from the trading activities of the appellant-company and had no relation to the capital value of the assets.
13.	***Commissioner of Income Tax, Bombay City I vs. CIBA India Ltd., (1968) 69 ITR 692 (SC).***	Contribution payable by the assessee at the rate of 6% of the net selling price, to the Swiss Company, on receiving the formula, scientific data, working rules and prescriptions pertaining to the manufacturing and processing of products discovered and developed in the Swiss Company's laboratories.	**Revenue expenditure**	That the assessee did not become entitled, even for the period of the agreement to the patents and trademark of the Swiss Company. That the assessee merely had a licence to trade and access to the patents and trademark of the Swiss Company for the limited period of the agreement. That the assessee did not acquire any asset or advantage of enduring nature.

14.	***Jabbar (M.A.) vs. Commissioner of Income Tax, Andhra Pradesh, (1968) 68 ITR 493 (SC).***	Payment made for a short term lease of eleven months for quarrying and to carry away, sell and dispose of sand which was lying on the surface of a river bed.	**Revenue expenditure**	That the lease was for a short period and the expenditure incurred by the assessee was not related to the acquisition of an asset or of a right of enduring nature, but merely to obtain stock-in-trade in the form of sand.
15.	***Lakshmiji Sugar Mills Co. Pvt. Ltd. vs. Commissioner of Income Tax, (1972) 82 ITR 376 (SC).***	Expenditure incurred on construction and development of roads between different sugarcane producing centres and sugar factories.	**Revenue expenditure**	That the said expenditure was incurred for the purpose of providing ease of transportation to the assessee and facilitating the assessee's business. There was no evidence to show that without such roads, the assessee would be unable to carry on business. Therefore, the expenditure was incurred merely for commercial expediency.

16.	***Devidas Vithaldas and Co. vs. C.I.T., Bombay City, (1972) 3 SCC 457.***	Purchase price (as a percentage of profits), paid on acquisition of a running business, as consideration for the right to use the goodwill of the business.	**Revenue Expenditure**	That the transaction did not amount to the sale of goodwill, as the duration of the payment as also the amount of consideration was indefinite as they depended on the rise and fall in the profits of the business. It was held that where the acquisition is not of the goodwill itself but for the rights to use it, the expenditure in the nature of royalty would be a revenue expenditure.
17.	***Mewar Sugar Mills Ltd. vs. CIT, (1973) 3 SCC 143.***	i. Payment made by the assessee to acquire monopoly rights to manufacture sugar in Udaipur; ii. 2% royalty paid to the ruler of Udaipur State on the price of the sugar manufactured.	**Payment of two percent royalty** on the sugar manufacture was held to be **revenue expenditure** while the **payment made in respect of the monopoly rights** obtained was held to be of **capital nature.**	That payment of the two per cent royalty on the price of sugar manufactured by the appellant therein had no relationship with the payment in reference to the monopoly conferred under the grant

18.	***Empire Jute Co. Ltd vs. Commissioner of Income Tax, (1980) 124 ITR 1 (SC).***	Payment made by the assessees for purchase of loom hours, and for allotment of hours of work per week, under a contractual agreement between various mills, restricting the right of every mill to work at full capacity.	**Revenue Expenditure**	The payment made by the assessees for purchase of loom hours was held to be expenditure incurred as part of the process of profit earning. The said expense was categorised as an outlay of a business in order to carry it on and to earn profit out of the expense. It was concluded that the expense was a part of the cost of operating the profit earning apparatus and was clearly in the nature of revenue expenditure.
19.	***L.H. Sugar Factory and Oil Mills Pvt. Ltd. vs. Commissioner of Income Tax, U.P., (1980) 125 ITR 293.***	i Assessee's contribution towards the construction of a dam, pursuant to the request of the Collector; ii. Expenditure incurred by the assessee towards the construction of roads in the area around its factory, under a Sugarcane Development Scheme floated by the State Government.	**i. Merely an act of good citizenship and not deductible expenditure".** **ii. Revenue expenditure**	i. That the assessee's contribution towards the construction of a dam, carried no advantage for the business of the assessee. The same was contributed without any obligation to do so and was simply an act of good citizenship and hence not deductible. ii. That construction of around the assessee's factory would be considerably advantageous to the business of the assessee as it would facilitate transport

				of sugarcane into the factory and manufactured sugar out of the factory. Hence, such expenditure was indubitably connected with the business activity of the assessee.
20.	***Commissioner of Income Tax vs. Associated Cement Companies Ltd., (1988) 172 ITR 257 (SC).***	Expenditure incurred by the assessee under a tripartite agreement with the State Government and Municipality of Shahabad, to supply water and electricity to Shahabad and to concrete the road from the factory to the railway station. In consideration of these amenities to be provided by the assessee company, the assessee secured immunity from payment for a period of 15 years.	**Revenue expenditure**	That the advantage secured by the assessee by making the expenditure was the securing of absolution or immunity from liability to pay municipal rates and taxes for a period of fifteen years. If these liabilities had been paid, the payments would have been on revenue account and hence the advantage secured was in the field of revenue and not capital. As a result of the expenditure there was no addition to the capital assets of the assessee company and no change in its capital structure. The pipelines which came into existence as a result of the expenditure belonged to the Municipality.

21.	***Alembic Chemical Works Co. Ltd. vs. Commissioner of Income Tax, Gujarat (1989) 177 ITR 377 (SC).***	One-time payment made under an agreement with a foreign firm by the assessee to obtain technical know how, for increasing yield of penicillin in its existing plant with a condition to keep the said know-how confidential	**Revenue expenditure**	First, that the expenditure was incurred for the purpose of existing day-to-day business, i.e., manufacture of penicillin and not for an entirely new venture unconnected or different from the existing business; Second, that given the rapid advancements in the field of medicine, a degree of durability and permanence cannot be attributed to the technical knowhow, particularly when it is not a case of exclusive acquisition.
22.	***Jonas Woodhead and Sons. India Ltd. vs. Commissioner of Income Tax, (1997) 224 ITR 342 (SC).***	i. Payment made towards accessing the know-how and technical information regarding the setting up of a plant; ii. Payment in the form of royalty for the services to be rendered to the assessee by the foreign firm.	**The consolidated payments made were apportioned and 25% thereof was held to be in the nature of capital expenditure while 75%, payable on services, was held to be revenue expenditure.**	Under the agreement with the foreign company, what was set up by the assessee was a new business and the foreign company had not only furnished information and technical know-how but had also rendered valuable services in the setting up of the factory itself. That even after expiry of the agreement there was no embargo on the assessee to continue to manufacture the product.

23.	***Commissioner of Income Tax vs. Madras Auto Services Pvt. Ltd., (1998) 233 ITR 468 (SC).***	Expenditure incurred by the assessee on demolishing an existing building and constructing a new building, during the subsistence of a 39 year lease, whereafter, the assessee continued to be a lessee in the building which belonged to the lessor.	**Revenue expenditure**	That the asset created, though of an enduring nature, did not belong to the assessee.
24.	***Honda Siel Cars India Ltd. vs. Commissioner of Income Tax, Ghaziabad, (2017) 8 SCC 170.***	Lump-sum fee payable by the assessee to M/s Honda Motors Company Ltd., Japan in five continuous instalments after commencement of commercial production of Honda cars by the assessee, under a licensing and technical assistance agreement between the parties.	**Revenue expenditure**	That the payment was made by the assessee, not to set up the plant to manufacture Honda cars but so as to obtain the licence to manufacture Honda cars in India, which were its stock in trade. That the agreement was framed in a manner as to give licence for a limited period, having no enduring nature.

Details of certain decisions of various High Courts, which have also been considered are presented in the table hereinbelow:

Sl. No.	***Cause Title and Citation***	***Transaction in Question***	***Classification of the Transaction in question by the High Court:***	***Reasons for classification:***
1.	Mohan Meakin Breweries Ltd. vs. Commissioner of Income Tax, (1997) 220 ITR 878. (High Court of Himachal Pradesh, Shimla)	Annual payment made to the State towards licence fee for working/ operating of a distillery.	Capital expenditure	That but for the licence so obtained, the assessee could not have established the distillery.
2.	Commissioner of Income Tax vs. Sarada Binding Works, (1976) 102 ITR 187 (Madras High Court)	i. Payment made by the assessee, of a fixed sum of Rs. 5000/- per annum to acquire the right to run the business of 'Chandamama Publications'; ii.Royalty paid annually on sales equivalent to 10% of the annual net profits.	**i. The expenditure incurred towards the right to run the business of 'Chandamama Publications' was held to be Capital expenditure; ii. Royalty was held to be in the nature of revenue expenditure.**	That payments calculated as a certain percentage of profits of a business for an indefinite period of time cannot be treated as payments by instalments of a capital sum. The payment of royalty was related to the future profits of the assessee and had no nexus with the capital sum.

3.	***Commissioner of Income Tax vs. Southern Switch Gear Ltd., (1984) 148 ITR 272*** (Madras High Court) ***Decision affirmed by this Court in Southern Switch Gear Ltd. vs. CIT, (1998) 232 ITR 35 (SC).***	i. Payment of technical collaboration/ technical aid fees by the assessee to a foreign company; ii. Royalty payable in five instalments for the acquisition of an exclusive privilege of manufacturing and selling the products.	**i. Technical collaboration fee was held to be capital expenditure;** **ii. 25% of the royalty was held to be capital in nature, while 75% was stated to be revenue expenditure.**	That by making a payment of royalty, the assessee had acquired an exclusive privilege to manufacture and sell the products. Therefore, the said expenditure was to be treated partly as capital and partly revenue. The value of the royalty related to the acquisition of the right of enduring nature was estimated at 25% and treated as capital expenditure, while the rest was stated to be revenue expenditure.
4.	***CIT vs. Saw Pipes Ltd., (2008) 300 ITR 35 (High Court of Delhi)***	Service charges paid by the assessee to Maharashtra State Electricity Board (MSEB) to set up a service line for supplying electricity, as part of an arrangement wherein the ownership of the cables would remain with the MSEB.	**Revenue expenditure**	That the service lines did not belong to the assessee but to the MSEB and were laid out to enable the assessee to conduct its business more effectively. Hence, the same was to be regarded as revenue expenditure.

5.	***CIT vs. J.K. Synthetics, (2009) 309 ITR 371*** (High Court of Delhi)	Payment made by the assessee under an agreement to access technical information of a foreign company, whereby there would be no transfer of ownership of the know-how in favour of the assessee, and the access was granted on a non-exclusive basis.	Revenue expenditure	That the assessee only acquired "access" to the technical information which related to the process of manufacture, which was not related to any secret process or intellectual property rights. The products in question were already being manufactured by the assessee and the know-how would only increase the assessee's profitability. Therefore, the expenditure would be in the nature of revenue expenditure.
6.	***Commissioner of Income Tax vs. Sharda Motors, (2009) 319 ITR 109*** (High Court of Delhi)	Royalty payable annually by the assessee, on the number of pieces manufactured, to a Korean Co. which had provided technical know-how to the assessee.	**Revenue expenditure**	That since royalty was payable on the quantity of the good produced, the same would be revenue expenditure.

7.	***CIT vs. Modi Revlon Pvt. Ltd., 2012 SCC OnLine Del 4463*** (High Court of Delhi)	Royalty consideration paid by the assessee annually, as a percentage of sales price, to Revlon Mauritius Ltd. for supply of technical know-how to manufacture goods.	Revenue expenditure	That notwithstanding the fact that the assessee was the sole licencee of the brand within a given territory, expenditure would be revenue in nature because the ownership of the brand continued to be with Revlon Mauritius. That there was nothing in the agreement suggestive of any vesting of the know-how or part of it, or the goodwill of the brand, in the assessee.

16. We may also refer to some decisions of the Courts in England, with a view to cull-out certain tests, which, although should not be treated as over-exacting, may suggest some broad and general guidelines to ascertain as to which side of the line the outlay in any particular case might reasonably be held to fall.

16.1. ***The City of London Contract Corporation Ltd. vs. Styles, (1887) 2 TC 239*** is the first of the line of cases where courts in England considered the issue as to the categorisation of expenditure, as capital or revenue. Bowen, L.J. broadly indicated that the outlay on the "acquisition of the concern" would be capital while an outlay in "carrying on the concern" is revenue.

16.2. In ***Vallambrosa Rubber Co. Ltd. vs. Farmer, (1910) 5 T.C. 529,*** Lord Dunedin observed that a proposition could be stated "in a rough way", to the effect that capital expenditure is a thing that is going to be spent once and for all and income expenditure is a thing which will incur every year.

This test was adopted by Rowalatt J. in ***Ounsworth (Surveyor of Taxes) vs. Vickers Ltd., (1915) 3 K.B. 267 ("Vickers Ltd.")*** wherein it was observed that the real test was between expenditure which was made to meet a continuous demand for expenditure as opposed to an expenditure which was made once and for all. In the course of the judgment however, it was suggested that what was determinative was whether the particular expenditure could be put against any particular work or whether it was to be regarded as an enduring expenditure to serve the business as a whole.

16.3. The latter guideline laid down in ***Vickers Ltd.*** served as the foundation for the test prescribed by Viscount Cave L.C. in the oft-cited case on the subject, ***British Insulated Helsby Cables Ltd. vs. Atherton, (1926) AC 205 ("Atherton"),*** wherein it was observed that when an expenditure is made, not only once and for all, but with a view to bringing into existence an asset or an advantage for the enduring benefit of trade, such an expenditure is property attributable to capital and not to revenue.

16.4. The expression *"enduring benefit of a trade"* was further explained as meaning not *"everlasting"*, but *"in the way capital endures"* vide Du Parcq, L.J., in ***Henriksen vs. Grafton Hotel Ltd., (1942) 24 T.C. 453.*** In the said case, Lord Greene stated that if the sum payable is not in the nature of revenue expenditure, it cannot be made so by permitting it to be paid by annual instalments. The payments by instalments in respect of monopoly value do not have the quality of annual payments or the grant of the annual excise licence, but are of a different character altogether.

16.5. Viscount Haldane however, in ***John Smith & Son vs. Moore, (1921) 12 T.C. 266,*** suggested another test- the test of fixed or circulating capital. Fixed capital being what the owner turns to profit by keeping in his possession; circulating capital is what the assessee makes profit from by parting or letting the product/asset change hands. However, in the said case, it was observed that the demarcation line between assets out of which profits were earned and the profit made upon assets or with assets, was thin and difficult to draw in several cases.

16.6. It was clarified in ***Mallet vs. Staveley Coal and Iron Co., (1928) 2 K.B. 405 ("Mallet")*** that where the expenditure is to bring into the hands of the company a necessary ingredient of their existing business, which is important but still ancillary to the business, the expenditure is to be debited to the circulating capital rather than to the fixed capital, which is employed in and sunk in the permanent assets of the business.

16.7. The test of fixed or circulating capital was also adopted by Lord Hanworth, M.R. in ***Anglo-Persian Oil Co. vs. Dale, (1932) 1 K.B. 124 ("Dale")*** wherein it was observed:

> "I am inclined to think that the question whether the money paid is provided from the fixed or the circulating capital comes as near to accuracy as can be suggested."
>
> In further elucidation of the principle, it was laid down as follows:
>
> a) The expenditure is to be attributed to capital if it be made "with a view" to bringing an asset or advantage into existence, however, it is not necessary that it should always achieve the intended result in order to be held to be capital in nature. Thus the sum spent in trying to procure an agency agreement or a licence, may be capital expenditure though the intended agency or licence may not be ultimately secured.
>
> b) By 'enduring', it is meant "enduring in the way that fixed capital endures" and it does not connote a benefit that endures in a sense that for a good number of years it relieves the assessee of a revenue payment.

However, in ***Van Den Berghs, Limited vs. Clark (H.M. Inspector of Taxes), (1935) 19 T.C. 390,*** Lord Macmillan veered round to the test of enduring benefit and expressed reservations regarding the test of fixed and circulating capital. That *"where the character of the expenditure shows that what has resulted is something which is to be used in the way of business, the test may be useful; but in cases close to the dividing line, the test seems useless."*

16.8. A third test was propounded in ***Robert Addie & Sons Collieries Ltd. vs. Commissioners of Inland Revenue, (1924) 8 T.C. 671,*** while determining whether a given expenditure is capital or revenue in nature:

> "Is it part of the Company's working expenses, is it expenditure laid out as part of the process of profit-earning? or, on the other hand, is it a capital outlay, is it expenditure necessary for the acquisition of

property or of rights of a permanent character, the possession of which is a condition of carrying on its trade at all?"

The said test was adopted by the Privy Council in ***Tata Hydro-Electric Agencies Ltd., Bombay vs. Commissioner of Income-tax, (1937) L.R. 64 IndAp 215*** wherein it was stated that the expenditure which is part of the working expenses in ordinary commercial trading was not capital but revenue. It was further observed that the determinative question would be whether the expenditure is *"a part of the company's working expenses; is it expenditure laid out as part of the process of profit earning ?"*

Referring to the facts of the said case, the Privy Council came to the conclusion that the obligation to make the payments was undertaken by the appellants therein in consideration of their acquisition of the right and opportunity to earn profits, i.e., of the right to conduct the business and not for the purpose of producing profits in the conduct of the business. The distinction was thus made between the acquisition of an income-earning asset and the process of the earning of the income. Expenditure in the acquisition of that asset was capital expenditure and expenditure in the process of the earning of the profits was revenue expenditure. It was further observed that on acquisition of a business and when a liability to pay yearly sums is taken over, those yearly sums were not deductible in computing future profits for tax purposes, as they form a part of the consideration for the acquisition of the business.

16.9. A similar guideline was expressed in ***Sun Newspapers Limited and the Associated Newspapers Limited vs. The Federal Commissioner of Taxation, (1938) 61 C.L.R. 337,*** wherein it was stated that the expenditure incurred towards establishing, replacing and enlarging the profit yielding subject must be contrasted with the continual flow of working expenses, which ought to be supplied continually out of the returns of revenue. While the former category of expenditure would be capital in nature, the latter would be revenue. It was further held that while applying the 'enduring benefit' test the words, 'permanent' or 'enduring' are not to be understood to mean ever-lasting. The distinction which is drawn is that between more or less recurrent expenses involved in running a business and an expenditure for the benefit of the business as a whole.

16.10. Certain supplementary tests have been laid down by the Judicial Committee in ***Mohanlal Hargovind of Jubbulpore vs. Commissioner of Income Tax, (1949) L.R. 76 IndAp 235*** wherein the assessee had paid for purchasing tendu leaves from the forest, which right included the right of entry and coppicing and pollarding. The said expenditure was for acquiring the raw materials for the manufacturing business and thus a capital expenditure. In the said case, the assessee was a paid manufacturer who had obtained short-term contracts with the Government and other forest owners to obtain tendu leaves from the forests. The Judicial Committee held that these contracts were, in a business sense, for the purpose of securing supplies to the manufacturers of one of the raw materials of his business. They granted no interest in land or the plants or trees and therefore, the expense incurred in this regard was not a capital expenditure.

17. A study of the aforesaid decisions of the Courts of England would reveal that the following factors have guided the Courts in the said jurisdiction in determining the nature of transactions:

i. **Periodicity of payments:** In the broadest sense, capital expenditure is a thing that is going to be spent once and for all and income expenditure is a thing which will incur every year. However, expenditure which is not 'once and for all' may nevertheless be capital. Expenditure of a recurring nature on the acquisition of assets which are clearly fixed rather than circulating capital, remains capital. Moreover, an outgoing does not cease to be of a capital nature merely because it is payable in instalments, vide ***CIR vs. Adam, (1928) 14 T.C. 34.*** The test is therefore to determine, whether, the payment is made as a matter of such frequent recurrence that it is a part of ordinary working expenditure, ***Bonner vs. Basset Mines Ltd., (1912) 6 T.C. 145.***

ii. **Object of the expenditure:** The ***Atherton*** test looks to the purpose or motive of expenditure. For expenditure to be capital it must be spent for the acquisition, improvement or disposal of a capital asset, vide ***Rolfe vs. Wimpy Waste Management Ltd., (1989) 62 T.C. 399; Tucker vs. Granada Motorway Services Ltd., (1979) 53 T.C. 92 ("Tucker"); Mallet,*** respectively. However, the relationship between the expenditure and the acquisition, improvement or disposal of a capital asset must be proximate and not remote. For instance, payment made to staff could not be said to be payment made for acquisition of goodwill and hence capital in nature, although, the staff by serving well may help create the goodwill, *vide* ***Lawson vs. Johnson Matthey Plc., (1992) 65 T.C. 39.***

iii. **Identifiable asset test:** It is necessary to identify a specific capital asset for which the expenditure is incurred, vide ***Tucker***. When the asset is an intangible benefit (licences, trading agreements etc.) it will be necessary to ask whether the identifiable asset is of a sufficiently substantial and enduring nature to count as capital, vide ***Dale; CIR vs. Carron Company, (1968) 45 T.C. 18; Heather vs. PE Consulting Group Ltd., (1972) 48 T.C. 293.***

iv. **Expenditure on commercial advantages generally:** Expenditure on commercial advantages dependent on a particular trading relationship is likely to be capital only if a permanent advantage, such as the closing down of a potentially damaging competitor, is secured by the payment, ***Walker vs. The Joint Credit Card Co., (1982) 55 T.C. 617.*** However, expenditure which is incurred towards general business convenience (such as to facilitate transport, supply-chain management, obtain temporary advantage over a competitor etc.) is of revenue nature, ***CIR vs. Nchanga Copper Mines, (1964) 1 All ER 208 ("Nchanga Copper Mines").***

v. **Effect, if any, of the expenditure on the profit-making structure:** The question to consider is, whether, the payment was made with a view to earn profit in a new form, or to structure the assessee's profit making apparatus. While the former category of expenditure would be revenue in nature, the latter would be capital.

18. The test that was adopted, almost universally, in the early decisions in India, is akin to the one laid down by Viscount Cave L.C. in ***Atherton.***

18.1. In ***Commissioner of Income Tax, Bombay vs. Century Spinning, Weaving and Manufacturing Co., (1942) 10 ITR Suppl., M.C. Chagla J.*** observed that the legal touchstone which is most familiarly applied in the Indian context is that of Viscount Cave in ***Atherton's*** case.

18.2. ***In Benarsidas Jagannath, In re, (1946) 15 ITR 185,*** a Full Bench of the Lahore High Court attempted to reconcile the tests referred to hereinabove and deduced the following broad tests for distinguishing capital expenditure from revenue expenditure:

> "It is not easy to define the term 'capital expenditure' in the abstract or to lay down any general and satisfactory test to discriminate between a capital and a revenue expenditure. Nor is it easy to reconcile all the decisions that were cited before us for each case has been decided on its peculiar facts. Some broad principles can, however, be deduced from what the learned Judges have laid down from time to time. They are as follows :-
>
> 1. Outlay is deemed to be capital when it is made for the initiation of a business, for extension of a business, or for a substantial replacement of equipment : vide Lord Sands in ***Commissioners of Inland Revenue v. Granite City Steamship Company (1927) 13 T.C. 1, 14). In City of London Contract Corporation v. Styles ((1887) 2 T.C. 239),*** at page 243, Bowen, L.J. observed as to the capital expenditure as follows :
>
>> "You do not use it 'for the purpose of' your concern, which means, for the purpose of carrying on your concern, but you use it to acquire the concern."
>
> 2. Expenditure may be treated as properly attributable to capital when it is made not only once and for all, but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade : *vide* Viscount Cave, L.C., in ***Atherton v. British Insulated and Helsby Cables Ltd. ((1925) 10 T.C. 155).*** If what is got rid of by a lump sum payment is an annual business expense chargeable against revenue, the lump sum payment should equally be regarded as a business expense, but if the lump sum payment brings in a capital asset, then that puts the business on another footing altogether. Thus, if labour saving machinery was acquired, the cost of such acquisition cannot be deducted out of the profits by claiming that it relieves the annual labour bill, the business has acquired a new asset, that is, machinery. The expressions 'enduring benefit' or 'of a permanent character' were introduced to make it clear that the asset or the right acquired must have enough durability to justify its being treated as a capital asset.

3. Whether for the purpose of the expenditure, any capital was withdrawn, or, in other words, whether the object of incurring the expenditure was to employ what was taken in as capital of the business. Again, it is to be seen whether the expenditure incurred was part of the fixed capital of the business or part of its circulating capital. Fixed capital is what the owner turns to profit by keeping it in his own possession. Circulating or floating capital is what he makes profit of by parting with it or letting it change masters. Circulating capital is capital which is turned over and in the process of being turned over yields profit or loss. Fixed capital, on the other hand, is not involved directly in that process and remains unaffected by it."

19. It may be useful at this juncture, to attempt to cull out the broad principles/tests that have been forged and adopted by this Court from time to time, while determining whether a given expenditure is capital or revenue in nature:

i. Capital expenditure is one met with a view to bring into existence an asset for the enduring benefit of the trade. However, this rule is not applicable in every case. The nature of the advantage acquired has to be considered in the commercial sense and only when the advantage is in the capital field, deduction on the said expenditure could be disallowed by applying the enduring benefit test. If the advantage consists merely of facilitating trading operations or enabling the management or conduct of business more effectively or profitably, while leaving the fixed capital untouched, the said expenditure would be on revenue account, though the advantage may endure for an indefinite period, *vide* ***Empire Jute Co. Ltd.*** Therefore, the enduring benefit test is not conclusive and cannot be mechanically applied without considering the commercial aspect of the transaction involving the expenditure in question.

ii. Where the expenditure is made for the initial outlay or for extension of a business, or a substantial replacement of the equipment, it is capital expenditure. If the expenditure is for running the business or working it with a view to produce profits, it is revenue expenditure, *vide* ***Assam Bengal Cement Co. Ltd.*** What also follows from this test is that expenditure which relates to the very framework or structure or edifice of the taxpayer's business is capital expenditure.

iii. The fixed and circulating capital test provides that where the expenditure is to bring into the hands of the assessee a necessary ingredient of their existing business, which is important but still ancillary to the business, the expenditure is to be debited to the circulating capital (revenue account) rather than to the fixed capital (capital account).

iv. Where there is no enlargement of the permanent structure or of capital assets and the expenditure essentially relates to the operation or working of the existing apparatus, such an expenditure would be on revenue account, *vide* ***Empire Jute Co. Ltd.***

v. The question as to whether an expenditure is capital or revenue in nature is to be judged in every case in the context of business necessity or expediency. The first aspect to be considered is whether, the expenditure is a part of the assessee's working expenditure or a part of profit earning. Further, an inquiry must be made as to, whether, the expenditure was necessary to acquire a right of permanent character, the possession of which is a condition precedent for carrying on a particular trade. In the event that the answer to the first question is in the negative and the second question is in the affirmative, the expenditure is inarguably capital in nature. In this context, we are of the view that the decision of this Court in ***Alembic Chemical Works Co. Ltd.*** must turn on its own peculiar facts.

vi. Thus, the aspect to be considered is whether the expenditure is incurred for the purpose of the existing day-to-day business of the assessee, or with a view to commence an entirely new venture. Where the expenditure incurred is merely to enhance the productivity or profitability of an existing business, without making significant changes to the structure of the assessee's profit making apparatus, the same is revenue in nature. ***Alembic Chemical Works Co. Ltd.*** was decided on the above premise.

vii. It is not necessary that in all cases, once and for all payment would result in an enduring benefit, nor it is a firm rule that periodical payment would not carry with it an enduring benefit.

viii. Mere payment of an amount in instalments does not convert or change a capital payment into a revenue payment. Similarly, lump-sum payment can represent revenue expenditure if it is incurred for acquiring circulating capital though payment is made once and for all. Likewise, payment made in instalments can be for acquiring a capital asset, the price of which is paid over a period of time. Therefore, what is relevant is the nature of the original obligation and whether the subsequent payment made in instalments relates to or has a nexus with such original obligation or not. Where the subsequent payments, are towards a purpose which is identifiably distinct from the original obligation of the assessee, the same would constitute revenue expenditure. However, where each of the successive instalments relate to the same obligation or purpose, the cumulative expenditure would be capital in nature.

ix. The general principle that expenditure on the creation of a capital asset is on capital account applies only where the capital asset belongs to the assessee. An amount spent by the assessee may be deductible on revenue account even if it results in the acquisition of a capital asset by a third party, *vide* ***L.H. Sugar Factory and Oil Mills Pvt. Ltd. vs. Commissioner of Income Tax, U.P., (1980) 125 ITR 293.***

x. Another pertinent question to consider is, whether, the expenditure is incurred towards purchase of an asset, or merely of the right to use the asset for a given period of time on payment of a certain consideration for the period of intended use, *vide* ***Devidas Vithaldas and Co.*** Where the asset is not purchased or is not vested with the assessee, but the assessee has simply acquired a right to use the asset, the payment would be of revenue nature, *vide* ***CIT vs. Modi Revlon Pvt. Ltd., 2012 SCC OnLine Del 4463 ("Modi Revlon Pvt. Ltd.").***

Payment of royalty:

20. In the present case, before considering the issue as to categorisation of the variable licence fee payable as a percentage of gross revenue, it is also necessary to understand the distinction between a payment made to acquire a right, and payment of royalty in a broad sense. Stated in the most simplistic manner, acquisition of a right would mean purchase of an asset, tangible or intangible, for the enduring advantage of the purchaser. When a right is said to be acquired, it means that the ownership of the said right vests with the purchaser. By contrast, payment of royalty is to use a right or asset. The right or asset is not per se acquired by the person or entity authorised to use it but continues to vest with the owner of the right. In case of royalty, payment is made merely to secure the right to use an asset for a stipulated duration. When the payment of royalty ceases, in most cases, the right to use the asset also ceases. Most often, the amount of royalty to be paid is dependent on the annual sales *vide* ***Commissioner of Income Tax, Bombay City I vs. CIBA India Ltd., (1968) 69 ITR 692 (SC) ("CIBA India Ltd."); Modi Revlon Pvt. Ltd.;*** annual profits *vide* ***Travancore Sugars and Chemicals Ltd.;*** or such other variable. Further, in order to qualify as royalty, the payment must have no nexus with the acquisition of a capital asset, vide **Travancore Sugars and Chemicals Ltd.; Mewar Sugar Mills Ltd.**

20.1. The decision of this Court in ***Gotan Lime*** is highly instructive while attempting to draw a distinction between payment made to acquire a right, and payment of royalty for use of a right or asset. In the said case, this Court considered the issue as to the classification of the annual payment made by the assessee therein, in lieu of the right to excavate limestone in a certain area. This Court, while holding that the payment in question therein was revenue expenditure, reasoned that the payment was not for securing an enduring advantage but was a royalty payment in order to obtain raw material and hence, a revenue expenditure. The pertinent observations of this Court are extracted hereinunder:

> "We are of the opinion that in the present case the royalty payment is not a direct payment for securing an enduring advantage; it has relation to the raw material to be obtained. Ordinarily, a mining lease provides for a capital sum payment; but the fact that there is no lumpsum payment here cannot by itself lead to the conclusion that

yearly payments to be made under the mining lease have relation to the acquisition of the advantage. No material has been placed on the record as to how any part of the royalty must, in view of the circumstances of the case, be treated as premium and be referable to the acquisition of the mining lease."

The above dictum is clear on the aspect of the distinction between payment made to acquire a right and payment of royalty inasmuch as it lays down in express terms that if a payment is made, not towards securing an enduring advantage or asset, but towards a right to use an asset, the same would be royalty. It has further been stated in no unclear terms that where a payment is not referrable to the acquisition of a capital asset (particularly, mining lease in the said case), but only secures a right to use the asset, the same would be royalty and hence classifiable as a revenue expenditure.

20.2. Relying on the decision in ***Gotan Lime***, this Court in ***Mewar Sugar Mills Ltd.*** while considering a transaction wherein the assessee therein paid: (a) Lump-sum payment to acquire monopoly rights for manufacture of sugar in Udaipur; and (b) payment to the ruler of Udaipur State, at the rate of 2% of the price of the sugar manufactured, held that the payment of the 2% royalty on the price of sugar manufactured by the appellant therein had no relationship with the payment referable to the monopoly conferred under the grant and hence, it was in the nature of revenue expenditure.

20.3. Another ingredient of payment as royalty is that in most cases, it relates to and is dependent on the profit earned or sales made by working an asset, rather than the acquisition of the asset itself. Such periodic payments, particularly those which are based on turnover of profit and which are not related to any predetermined lump-sum are towards royalty and correctly deductible as revenue expenditure.

20.4. In ***CIBA India Ltd.,*** this Court held that payments made for the right to have access to technical knowledge and the fruits of continuing research and experience of a foreign company and to use its patents and trademarks would be chargeable on revenue account. This would demonstrate that even where technical know-how is a capital asset, amounts paid for its mere use, or for the use of a trademark, trade name or the right to manufacture and sell certain goods, are allowable as revenue expenditure in the nature of royalty as the payment is made for the use of the asset and not for its acquisition. In such cases, the payment of royalty, has no relation to the capital value of the asset authorised to be used.

21. In our view, the following considerations are immaterial in determining the question, as to, whether, a payment is a capital disbursement or in the nature of a revenue expenditure:

i. **Lump-sum and periodical payment:** Lord Greene in ***Inland Revenue vs. Williams, 11 ITR Suppl. 84*** famously remarked, *"There is no magic in the distinction between a lump-sum and periodic sums"*. That the expense is a periodic expense or a lump-sum payment is immaterial for the purpose of determining its nature. A lump-sum payment may be revenue expenditure, for instance, when it represents the commutation of a series of annual revenue payments; and a recurring periodic payment may be capital expenditure, for instance when it represents the payments by instalments of a capital sum, *vide* ***Assam Bengal Cement Co. Ltd.***

ii. **Magnitude of payment:** The magnitude of a disbursement is immaterial for the purpose of determining its nature, for, magnitude is a relative term, *vide* ***Prendergast vs. Cameron, 8 I.T.R. Suppl. 75 (HL).***

iii. **Entries in books of accounts:** That an item of expenditure is debited in an entity's books of account to revenue account is by no means conclusive of its nature. Businesses frequently prefer to debit to the revenue account, payments which are in their nature to be carried to capital account. Conversely, an assessee may be entitled to a revenue deduction in respect of expenditure which is capitalised in the accounts, *vide* ***India Cements vs. Commissioner of Income Tax, 60 I.T.R. 52 (SC).***

22. In considering whether an item of expenditure is of a capital or revenue nature, we reiterate that one must consider the nature of the concern, the ordinary course of business usually adopted in that concern and the object with which the expenditure is incurred, *vide* ***Assam Bengal Cement Co. Ltd.*** Attention must be paid not only to the form of the transaction, but also its

substance. Where the transaction takes the form of a contract or other deed, it depends upon a proper construction of the terms of the contract whether a payment made thereunder is a capital disbursement or revenue expenditure. The true nature of a transaction must be gathered by placing emphasis on the business aspect of the transaction. What is an outgoing of capital and what is an outgoing on account of revenue depends on what the expenditure is calculated to effect from the practical and business point of view. This aspect of the transaction is then, to be reconciled with juristic classification of the legal rights, if any, secured, employed, or exhausted in the process.

22.1. Therefore, what is material is the nature of right sought to be secured through the payment or transaction in question. The purpose towards which the expenditure is incurred must guide any attempt to categorise the expenditure. The structure or form of the transaction or the payment schedule is hardly suggestive of the nature of the transaction. Therefore, it cannot be axiomatically held that an expenditure which in its core, capital in nature, is actually to be treated as a revenue expenditure simply because the payment is structured in instalments.

22.2. The determinative test to identify whether an expenditure structured in the form of instalments is in the nature of a capital expenditure or revenue expenditure, would be to first assess whether the payment made either in lump-sum or in instalments relates to the acquisition or expansion of a capital asset, or by contrast, relates to the working of an asset to produce profits; whether the consideration payable towards the acquisition or expansion of a capital asset has simply been chopped up into smaller sums payable in instalments, for the sake of convenience. The dictum of this Court in ***Pingle Industries Ltd.,*** is relevant in this regard. In the said case, the majority judgment stated that the payment in question therein was made with a view to acquire a long-term lease and a right to mine stones, and the lease was conveyed to the assessee who had to extract the stones and convert them as a stock-in-trade. That the expenditure was incurred towards securing a capital asset from which, after extraction, stones could be converted into stock-in-trade. The payment, though periodic, in fact, was neither rent nor royalty but a lump-sum payment in instalments for acquiring a capital asset of enduring benefit to the assessee's trade. According to this Court *"it was really the entire sum chopped into small payments for his* *convenience."* Hence, the amount could not be described as a business expense, because the outgoings every month were not to be taken as spent over purchase of stones but in discharge of a singular original obligation to the jagir. These observations clearly establish the difference between a revenue expenditure on the one hand and capital expenditure incurred in instalments on the other hand.

22.3. Similarly, in ***Jalan Trading Co.,*** this Court while considering the issue as to classification of periodic payments of 75% profit share, as consideration under a deed of assignment, for the right to carry on business, held that the same would be capital expenditure. It was observed that the assessee therein was a new company and it had acquired under the contract the right to carry on a business on long- term basis subject to the renewal of the agreement on payment of 75% of its annual net profits. That since the assessee had acquired a capital asset (right to carry out the business of the assignor), any payment made towards securing such a right would be capital in nature. This dictum would clearly demonstrate that when an expenditure is in its core capital in nature, neither the fact that the same was paid in instalments, nor the fact that the quantum of expenditure was dependent on the revenue or profit of the assessee, would warrant a change in the classification of the transaction.

23. Before proceeding to consider the facts of the present case in light of the precedents discussed hereinabove, it is necessary to preface our views by stating that it is perhaps one of the most familiar arguments in Courts (particularly in matters involving an issue as to classification of expenditure or receipts), that the case at hand bears close resemblance to another case falling on one or the other side of the line, and must therefore be decided in the same manner. This thought was conveyed by Lord Radcliffe in ***Nchanga Copper Mines*** wherein it was pointed out that *"in considering allocation of expenditure between capital and income accounts, it is almost unavoidable to argue from analogy."* In that context, we must highlight the difficulty of relying on any single precedent in search for the true classification, and attempting to draw similarities between the facts of the said case and the facts of the case at hand. We think that the propositions made in earlier cases, if sought to be applied to a different case which the authors of those propositions did not have in mind, could lead to absurd results.

Further, it is trite that the words in a judgment must not be construed in the same manner as those in a legislation. Hence, it is neither wise nor suitable to extend the dictum of one case, premised on the facts of the said case, to another fact-situation which is seemingly similar but not really so. This is particularly so when there is no precedent which has been rendered in an identical fact situation, as is the case in the instant matters.

23.1. In such situations, the solution may not be found in any one precedent. It has to be derived from many aspects of the whole set of circumstances some of which may point in one direction, while some to the other. It is an appreciation of all guiding factors, premised in common business sense, which must provide the ultimate answer, rather than mere analogy or comparison. It is with such an approach that we shall proceed to consider the facts of the case at hand in light of certain precedents referred to or/and relied upon by the High Court of Delhi as well as those cited at the Bar.

23.2. We also wish to refer to the dictum of the King's Bench Division in ***Commissioners of Inland Revenue vs. Ramsay, 20 T.C. 79.*** The facts of the said case were that the assessee therein agreed to purchase a dental practice for a primary consideration of £15,000 subject to increase or diminution as therein provided. The primary price was to be satisfied by payment of £5000 on the exchange of the agreement, and as to the balance, by payment each year for ten years of a sum equal to 25% of the net profits of the practice for each year. If the amounts so paid over the ten years, were in the aggregate, more or less than the balance of the primary purchase price, that price was to be treated as correspondingly increased or diminished. The Court while considering an issue as to the classification of the payments made each year held that the annual sums paid under the agreement, were instalments of capital and were not admissible as revenue deductions.

23.3. Similarly, as discussed hereinabove, this Court in ***Jalan Trading Co.*** had the occasion to consider the issue pertaining to classification of an annual payment based on profit sharing towards the right to carry on business. This Court concluded that since the annual payment of 75% profit share was paid by the assessee in consideration of the right to carry on the business of the assignors, the payment would be capital in nature. In doing so, this Court examined the contention of the assessee therein that, since what was paid as consideration was not a pre-determined lump-sum amount but an annual payment out of profits, such a payment should be held to be revenue in nature. The three-Judge Bench of this Court rejected the said contention suggesting that when an expenditure is in its core capital in nature, neither the fact that the same was paid in instalments, nor the fact that the quantum of expenditure was dependent on the revenue or profit of the assessee, would warrant a change in the classification of the transaction.

This judgment will apply on all fours in deciding the case at hand, since the annual payment of variable licence fee is only towards licence fees and merely because it is paid in annual instalments based on the AGR, the payment cannot be construed as revenue. The annual payments of licence fee as also the entry fee relate to a singular purpose, i.e., the acquisition of the right to carry on the business of rendering telecommunication services. This right being in the nature of a capital asset, any payment(s) made towards the acquisition of the right, whether in lump-sum or in annual instalments dependent on the AGR, would be in the nature of capital disbursement(s).

23.4. This conclusion is also consistent with the view of this Court in ***Pingle Industries Ltd.,*** wherein by a majority of 2:1 held that the payment, towards acquisition of a long-term lease to win mine stones, though periodic, was neither rent nor royalty but a lump-sum payment in instalments for acquiring a capital asset of enduring benefit to trade. This Court refused to hold that the periodic payments were towards purchase of stones, but instead opined that the payments were in discharge of a singular original obligation to the jagir. Therefore, it emerges that where the periodic payments are referrable to or have a nexus with the original obligation undertaken by the assessee as consideration for acquisition of a right, the periodic payments would be in the nature of capital expenditure, notwithstanding the fact that they are payable as a percentage of profits, gross revenue or sales.

24. Hence, we are of the considered view that in the present case, since the entry fee as well as variable licence fees are traceable to the same source, they would both have to be held to be capital in nature, notwithstanding the fact that the variable licence fee is paid in a staggered manner. We shall consider the case law sought to be relied upon by the learned senior counsel and learned counsel for the respondents-assessees, so as to distinguish the same from the present case.

24.1. We shall first advert to the decision of this Court in ***Jonas Woodhead and Sons.*** Paragraph 2 of the said judgment, in no unclear terms captures two underlying transactions arising out of the agreement in the said case; the first transaction relating to the know-how and technical information regarding setting up of the plant and the second transaction relating to the services to be rendered to the assessee by the foreign firm, the consideration for the second prong being in the nature of royalty. It is in that backdrop that the consolidated payment was apportioned and 25% thereof was held to be in the nature of capital expenditure while 75%, payable on services, was held to be revenue expenditure.

Further, it is also relevant to note that in the said case the exercise of apportionment into the aforesaid fractions was carried out by the Madras High Court. Against the judgment of the High Court, the Revenue did not prefer an appeal before this Court on the findings pertaining to apportionment of 75% towards services. What was appealed against by the assessee was with regard to categorisation of 25% of the consolidated expenditure as capital expenditure. The assessee alone was the appellant before this Court. Therefore, the question as to apportionment of 75% towards services, was not considered and decided by this Court in the said case.

We are of the view that the judgment of this Court in ***Jonas Woodhead and Sons*** would not come to the aid of the respondent-assessees because the issue before this Court in the said case did not relate to a single right wherein the payment made towards the same was held to be partly capital and partly revenue. The purpose of payments in the said case was traceable to two different subject matters and therefore apportionment between capital and revenue expenditure. However, in the present case, the entry fee as well as variable licence fees are traceable to the same source.

24.2. Similarly, in ***Best and Co.,*** this Court decided the nature of expenditure on two separate transactions, though payments made were consolidated in nature. The first transaction related to the compensation paid by the principal for the termination of agency business, while the second was with respect to the payment made towards the non-compete clause. On the first aspect, namely, the compensation received for the loss of agency, it was held that what would be determinative was whether loss of agency would affect the entire business structure, resulting in a loss of enduring nature, or, whether it was a loss due to an ordinary incident in the course of business. If it was the former, it would be capital, and if it was the latter, it would be revenue in nature. It was concluded vis-à-vis the first transaction that the loss of the said agency by the assessee was only a normal trading loss and therefore the income received in this regard was a revenue receipt. As regards the non-compete clause it was held that the same was a restrictive covenant and was therefore, capital in nature. In paragraph 14 of the judgment of this Court, it was recorded in unequivocal terms that the *"compensation paid was in respect of two distinct matters, one taking the character of a capital receipt and the other of a revenue receipt."* Therefore, ***Best and Co.*** is a case where two independent transactions were considered, one of which was held as capital and the other as revenue. This case did not decide the expenditure towards the same right to be partly capital and partly revenue.

24.3. We shall now consider the decision of the Madras High Court affirmed by this Court in ***Southern Switch Gear Ltd.*** Paragraph 2 of the judgment of the High Court records two distinct transactions: one, for provision of technical know-how for the manufacture of switch gear products and the second, was to share modern developments and also train necessary personnel in the factory in United Kingdom. The consideration was fixed £20,000 payable in five instalments of £4000 each. Paragraph 5 of the judgement of the High Court referred to clause 6 of the agreement which dealt with know-how and clause 7 thereof, which dealt with supervision and direction, besides recommending appointment or dismissal of employees and also training them in the factory. In paragraph 6, it was held that expenditure on technical know-how is capital in nature and should be apportioned at 25% and the services rendered relatable to 75% of the consideration was revenue in nature. When the assessee therein filed an appeal before this Court against the finding that technical know-how is capital in nature and should be apportioned at 25%, the appeal was dismissed.

Therefore, it is clear that the said case also did not pertain to one source of expenditure being split, partly as capital and partly as revenue in nature. In the said case, the Courts have examined two different constituents of expenditure and held one component to be capital in nature while the other to be revenue in nature.

24.4. Next, we advert to the facts in ***Sarada Binding Works*** on which heavy reliance was placed by learned senior counsel Mr. Datar. The agreement relevant to the said case envisaged conveyances of two aspects: first, the right to run the business of 'Chandamama Publications' on payment of a fixed sum of Rs. 5000/- per annum; second, royalty to be paid annually on sales equivalent to 10% of the annual net profits. The High Court held that the right to run the business is capital in nature, whereas, the sharing of 10% profit per annum is revenue in nature. In the concluding paragraph, the High Court made the following firm conclusions as to why 10% profit sharing would constitute a revenue expenditure:

i. That payments calculated as a certain percentage of profits of a business for an indefinite period of time as royalty cannot be treated as payments by instalments of a capital sum;

ii. The payment of royalty was related to the future profits of the assessee and had no nexus with the capital sum.

In the said case, there are clear findings to the effect that the payment of royalty in instalments, in the absence of any definitive duration, cannot be linked to the right to carry on trade. That the payment of royalty had no nexus with the capital sum. However, in the present case, it cannot be said that the variable licence fee payable annually has no nexus with the acquisition of the capital asset, i.e., the licence to render telecom services, as, it is the payment of entry fee as well as the variable licence fees which together enable the assessees to carry on the said business. Hence the aforesaid case would not apply to the present case having regard to its distinct facts.

24.5. Sri Datar has also sought to rely upon the decision of this Court in ***Mewar Sugar Mills Ltd.*** However, we do not see how this judgment would bolster up the respondents' case. In the said case, the grant of licence by an agreement dated 05 April, 1932 contemplated two different aspects: first, a monopoly right to cultivate sugarcane and produce sugar, and second, payment of 2% royalty on the price of the sugar manufactured. In that backdrop, this Court held that the payment of 2% royalty on the sugar manufactured was revenue expenditure while the payment made in respect of the monopoly rights obtained was of capital nature. It was observed that payment of the 2% royalty on the price of sugar manufactured by the appellant therein had no relationship with the payment referable to the monopoly conferred under the grant.

In the said case, this Court's dictum is clear to the effect that royalty based on manufacture was in no way connected to the acquisition of monopoly rights. But such a finding would be erroneous in the facts of the present case since what is paid is only for acquisition of a right by way of licence fee. Further, in the said case, royalty payment had been divorced from the payment for the right to carry on business since any failure to pay royalty could not have, by any stretch, resulted in the withdrawal of the right to carry on trade. The right to carry on trade would have remained unaffected whether or not royalty payment was made. Failure to make royalty payment, could have at the most, led to civil consequences, but not a revocation of the right to carry on trade, whereas, in this batch of matters, the position is not the same. Admittedly, any failure to pay the annual variable licence fee will inevitably lead to revocation of the licence under Section 8 of the Telegraph Act. Further, the respondents will be disabled from carrying on the business of offering telecommunication services, even for a day in the absence of a valid licence. Continuation of the right to carry on the said business is contingent on the payment of both, entry fee, as well as variable licence fee.

Therefore, we are unable to rely upon the dictum in ***Mewar Sugar Mills Ltd.*** to hold in favour of the respondent-assessees in this batch of cases.

25. In light of the aforesaid discussion and having regard to the tests and principles forged by this Court from time to time, as detailed in paragraphs hereinabove, we shall proceed to consider whether the High Court of Delhi was right in apportioning the licence fee as partly revenue and partly capital by dividing the licence fee into two periods, i.e. before and after 31 July, 1999 and accordingly holding that the licence fee paid or payable for the period upto 31 July, 1999 i.e. the date set out in the Policy of 1999 should be treated as capital and the balance amount payable on or after the said date should be treated as revenue.

We answer the said question in the negative, against the assesses and in favour of the Revenue for the following reasons:

i. Reliance placed by the High Court on the decisions of this Court in ***Jonas Woodhead and Sons*** and ***Best and Co.*** and the decision of the Madras High Court in ***Southern Switch Gear Ltd.*** as approved by this Court appear to be misplaced inasmuch as the said cases did not deal with a single source/purpose to which payments in different forms had been made. On the contrary, in the said cases, the purpose of payments was traceable to different subject matters and accordingly, this Court held that the payments could be apportioned. However, in the present case, the licence issued under Section 4 of the Telegraph Act is a single licence to establish, maintain and operate telecommunication services. Since it is not a licence for divisible rights that conceive of divisible payments, apportionment of payment of the licence fee as partly capital and partly revenue expenditure is without any legal basis.

ii. Perhaps, the decision of the High Court could have been sustained if the facts were such that even if the respondents-operators did not pay the annual licence fee based on AGR, they would still be able to hold the right of establishing the network and running the telecom business. However, such a right is not preserved under the scheme of the Telegraph Act which we have detailed above. Hence, the apportionment made by the High Court is not sustainable.

iii. The fact that failure to pay the annual variable licence fee leads to revocation or cancellation of the licence, vindicates the legal position that the annual variable licence fee is paid towards the right to operate telecom services. Though the licence fee is payable in a staggered or deferred manner, the nature of the payment, which flows plainly from the licensing conditions, cannot be recharacterized. A single transaction cannot be split up, in an artificial manner into a capital payment and revenue payments by simply considering the mode of payment. Such a characterisation would be contrary to the settled position of law and decisions of this Court, which suggest that payment of an amount in instalments alone does not convert or change a capital payment into a revenue payment.

iv. It is trite that where a transaction consists of payments in two parts, i.e., lump-sum payment made at the outset, followed up by periodic payments, the nature of the two payments would be distinct only when the periodic payments have no nexus with the original obligation of the assessee. However, in the present case, the successive instalments relate to the same obligation, i.e., payment of licence fee as consideration for the right to establish, maintain and operate telecommunication services as a composite whole. This is because in the absence of a right to establish, maintenance and operation of telecommunication services is not possible. Hence, the cumulative expenditure would have to be held to be capital in nature.

v. Thus, the composite right conveyed to the respondents-assessees by way of grant of licences, is the right to establish, maintain and operate telecommunication services. The said composite right cannot be bifurcated in an artificial manner, into the right to establish telecommunication services on the one hand and the right to maintain and operate telecommunication services on the other. Such bifurcation is contrary to the terms of the licensing agreement(s) and the Policy of 1999.

vi. Further, it is to be noticed that even under the 1994 Policy regime the payment of licence fee consisted of two parts:

a) A fixed payment in the first three years of the licence regime;

b) A variable payment from the fourth year of the licence regime onwards, based on the number of subscribers.

Having accepted that both components, fixed and variable, of the licence fee under the 1994 Policy regime must be duly amortised, there was no basis to reclassify the same under the Policy of 1999 regime as revenue expenditure insofar as variable licence fee is concerned.

26. As per the Policy of 1999, there was to be a multi-licence regime inasmuch as any number of licences could be issued in a given service area. Further, the licence was for a period of twenty years instead of ten years as per the earlier regime. The migration to the Policy of 1999 was on the condition that the entire policy must be accepted as a package and consequently, all legal proceedings and disputes relating to the period upto 31 July, 1999 were to be closed. If the migration to the Policy of 1999

was accepted by the assessees herein or the other service providers, then all licence fee paid upto 31 July, 1999 was declared as a one time licence fee as stated in the communication dated 22 July, 1999 which was treated to be a capital expenditure. The licence granted under the Policy of 1999 was non-transferable and non-assignable. More importantly, if there was a default in the payment of the licence fee, the entire licence could be revoked after sixty days notice. The provisions of the Telegraph Act particularly Section 8 thereof are also to the same effect. Having regard to the aforesaid facts and in light of the aforesaid conclusions, we hold that the payment of entry fee as well as the variable annual licence fee paid by the respondents-assessees to the DoT under the Policy of 1999 are capital in nature and may be amortised in accordance with Section 35ABB of the Act. In our view, the High Court of Delhi was not right in apportioning the expenditure incurred towards establishing, operating and maintaining telecom services, as partly revenue and partly capital by dividing the licence fee into two periods, that is, before and after 31 July, 1999 and accordingly holding that the licence fee paid or payable for the period upto 31 July, 1999 i.e. the date set out in the Policy of 1999 should be treated as capital and the balance amount payable on or after the said date should be treated as revenue. The nature of payment being for the same purpose cannot have a different characterisation merely because of the change in the manner or measure of payment or for that matter the payment being made on annual basis.

27. Therefore, in the ultimate analysis, the nomenclature and the manner of payment is irrelevant. The payment post 31 July, 1999 is a continuation of the payment pre 31 July, 1999 albeit in an altered format which does not take away the essence of the payment. It is a mandatory payment traceable to the foundational document i.e., the license agreement as modified post migration to the 1999 policy. Consequence of non-payment would result in ouster of the licensee from the trade. Thus, this is a payment which is intrinsic to the existence of the licence as well as trade itself. Such a payment has to be treated or characterized as capital only.

28. In the result, the judgment of the Division Bench of the High Court of Delhi, dated 19 December, 2013 in ITA No. 1336 of 2010 and connected matters, is hereby set aside. The judgments passed by the High Courts of Delhi, Bombay and Karnataka, following the judgment of the

Division Bench of the High Court of Delhi, dated 19 December, 2013, are also consequently set aside.

The appeals filed by the appellant(s)-Revenue are allowed.

Parties to bear their respective costs.

Pending applications, if any, stand disposed of in the aforesaid terms.

Appeals allowed.

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