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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

+ **ITA 238/2024**

PR. COMMISSIONER OF INCOME TAX, DELHI -7

..... Appellant

Through: Mr. Puneet Rai, Sr. SC
alongwith Mr. Ashvini Kumar,
Mr. Rishabh Nangia and Mr.
Nikhil Jain, Advocates

versus

TIKONA INFINET LIMITED

..... Respondent

Through: Mr. Vipul J. Shah, Advocate

CORAM:

HON'BLE MR. JUSTICE YASHWANT VARMA

HON'BLE MR. JUSTICE PURUSHAINDR KUMAR

KAURAV

ORDER

14.05.2024

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**CM APPL. 24563/2024 (delay in filing) & CM APPL. 24564/2024
(delay in re-filing)**

Bearing in mind the disclosures made, the delay of 48 days in filing the appeal and the delay of 130 days in re-filing the appeal is condoned.

The applications shall stand disposed of.

ITA 238/2024

1. The Principal Commissioner has approached this Court questioning the validity of the judgment rendered by the Income Tax Appellate Tribunal ["ITAT"] on 24 April 2023.
2. The solitary question which stands posited for our consideration reads as follows:-



“I. Whether on facts and circumstances of the case and in law, Hon'ble ITAT was justified in deleting the addition of Rs.3,90,40,000/- made by the Assessing Officer on account of disallowance of annual fee (license fee) treating as capital expenditure for the A.Y 2010-11?”

3. Having heard Mr. Rai, learned counsel appearing in support of the appeal and on going through the judgment rendered by the Supreme Court in **CIT, Delhi v. Bharti Hexacom Ltd.** [2023 SCC OnLine SC 1340], we are of the considered opinion that the issue framed stands answered in favour of the appellant.

4. We deem it appropriate to extract the following passages from the decision in *CIT v. Bharti Hexacom Ltd.* :-

“89. 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. v. 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 v. Modi Revlon Pvt. Ltd.*, 2012 SCC OnLine Del 4463 (“*Modi Revlon Pvt. Ltd.*”).

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97. 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.

98. 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.

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105. 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.

106. 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).

107. 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 referable 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.



108. 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....”

5. In the backdrop of the aforesaid findings, we accordingly allow the instant appeal and set aside the order of the ITAT to the extent of disallowance of licence fee and which was liable to be treated to be “capital expenditure”.

YASHWANT VARMA, J.

PURUSHAINDRA KUMAR KAURAV, J.

MAY 14, 2024

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