

CALCUTTA HIGH COURT

Sri Annapurna Cotton Mills Ltd

Vs

Commissioner of Income-Tax

(Sinha ,J .)

04.12.1962

JUDGMENT

Sinha J

1. This is preference under section 66(1) of the Income-tax Act. The facts are as follows : The assessee, Sri Annapurna Cotton Ltd., is a company with a limited liability. The assessment year is 1952-53 corresponding to the accounting year, being the calendar year 1951-52. The assessee company raised a loan of Rs. 10,00,000 by issuing debentures. A debenture trust deed, dated 26th January, 1950, was executed by and between the company and Kumar Promotha Nath Roy and others as trustees. A copy of the said deed has been annexed to the statement of case and appears at pages 8-37 of the proper-book. According to the trust deed, the debenture was redeemable by ten annual instalments of rupees one lakh each, commencing from 31st December, 1954, and ending on the 31st December, 1963, bearing interstate the rate of 7% per annum payable half-yearly. The company secured payment of principal and interest by charging the properties described in the first schedule to the indenture of trust. The first schedule consists of the landed properties, machinery, building, and stock-in-trade belonging to the company. On the same date, another agreement was entered into between company and one Jogendra Lal Nandi and Anil Krishna Pal. A copy of this agreement is annexed to the statement of case and appears at pages 5-7 of the paper-book. In this agreement, there is a recital that the company required a loan to the extent of rupees ten lakhs for erecting its mills and purchasing its plant and machinery and stock-in-trade and for running the mill. The agreement shows that Jogendra Lal Nandi and Anil Krishan Pal as brokers obtained the loan for the company, in consideration of a commission of 1% to be paid in perpetuity on the gross sale of the products of the mill of the company. Such payment was to be made immediately after expiry of each year, and the first of such payments was to be made immediately after 31st December, 1950. This commissioner was to be received by the said Jogendra Lal Nandi and Anil Krishna Pal and their respective heirs, executors, administrators, representatives and assignees in perpetuity. The said Jogendra Lal Nandi dies on

the 7th June, 1950. He was succeeded by his three sons, Sukumar Nandi, Kusum Kumar Nandi and Sudhir Kumar Nandi, and his widow, Sm. Rohini Nandi. They, together with Anil Krishna Pal, transferred or assigned their right to receive the commission in perpetuity to two other persons, namely, Sunil Kumar Pal and Amar Krishna Poddar, by a registered deed of assignment dated 10th December, 1951. In pursuance of the agreement with the company, it paid a sum of Rs. 21,798 during the assessment year to the said Sunil Kumar Pal and Amar Krishna Poddar. The company claimed the payment to be revenue expenditure, being a liability of the company incurred for the purpose of carrying out its business. The Appellate Tribunal held that the loan was term loan was certainly a liability, in the sense that it had to be repaid. But being a long term loan, it became a part of the assets of the company and being an asset of an enduring character, it must be considered as a capital asset. An expenditure incurred for securing capital of the nature mentioned above is to be regarded in law as an expenditure of a capital nature. Therefore, the Tribunal held that the amount paid was to be regarded as a capital expenditure and, consequently, not allowable under section 10(2)(xv) of the Indian Income-tax Act. Thereupon, a dispute has been raised and the following question has been referred to us under section 66(1) of the Income-tax Act :: Whether, on the facts and in the circumstances of the case, the sum of Rs. 21,798 was a capital expenditure and as such not allowable as a deduction under section 10(2)(xv) of the Indian Income-tax Act ?"The point for determination, therefore, is as to whether the payment of commission to brokers in the circumstances mentioned above is capital expenditure or a revenue expenditure allowable under section 10(2)(xv) of the Income-tax Act. Before proceeding to decide the question, I should like to set out the following summary of Mr. Meyers argument on behalf of the respondent :

- "1. Whether a commission to brokers for raising a loan is of a capital nature or revenue expenditure, depends on the nature of the loan.
2. Where a debenture loan is raised upon a security of properties belonging to the company, it is always of a capital nature, except in the case of a short term loan which becomes a part of the assessee's profit making structure.
3. The raising of a debenture even for the purpose of day-to-day carrying out of a business of the assessee would be a capital nature, inasmuch as it is indistinguishable from the raising of share capital.
4. In the present case, the commission payable is in respect of a long-term loan and regard being had to the purpose for which it has been raised and the manner of raising it, the loan itself must be taken to have formed a part of the capital assets of the company and the commission paid in connection therewith is expenditure of a capital nature and not allowable as revenue expenditure under section 10(2)(xv) of the Income-tax Act. In order to support these propositions, a number

of cases have been cited, some of which, I shall now proceed to consider. The first case, which upon the facts comes very near to the present one is a decision of the Queens Bench of England, *Texas Land & Mortgage Co. v. Holtham*. In that case, the company was registered in England and the memorandum of association authorised the raising of money, inter alia, by the issue of bonds, mortgages and debentures. During the three financial years commencing from 5th April, 1890, the company issued certain debentures and debenture stock. The expenses of the issue and placing of such debentures and debentures stock, inter alia, consisted of an item of commission and fees paid to brokers to the extent of Pound 5,055 4s. 10d. There were other items like stamps on debenture and incidental charges. The question arose whether such cost including the commission was expenditure of a capital nature or an allowable expense chargeable against the profits and gains of the company. The Commissioners for Inland Revenue were of the opinion that any cost incurred in the process of raising debentures and debenture stock was expenditure of a capital nature and was not an expense chargeable to revenue. Thereupon, the assessee asked for the question to be referred to court and it was so referred. It was argued that the fees paid to the brokers upon the issue of debentures formed part of the expenses in carrying on the business of the company, because, before they could lend money, they had to raise a capital. Viscount Cave, whose decisions relating to income-tax law is always authoritative, indicated his opinion that the commissioner for raising a debenture loan was "only so much capital. A man wants to raise Pound 100,000 of capital, and in order to do that he has to pay Pound 4,000. That makes the capital Pound 96,000. That is all."

"Learned counsel however argued that the capital of the company, properly so called, was the share capital and nothing else. Viscount Cave expressed his opinion that to the extent that the company borrowed money, it increased its capital. The judgment was delivered by Mathew J., which was a very short one and must be set out.

"There is no doubt that in this case this company raised money by shares with the intention of lending money on mortgage. To increase its capital it raised money on debentures. The argument is that the cost of capital raising the money ought to be deducted from the profits in a particular year. We are clearly of opinion that cannot be done. The amount paid in order to raise the money on debentures, comes off the amount advanced upon the debentures, and, therefore, is so much paid for the cost getting it, but there cannot be one law for a company having sufficient money to carry on all its operations and another which is content to pay for the accommodation. This appears to me to be entirely concluded by the decision of yesterday (*Anglo Continental Guano Works v. Bell*)."

In the case cited by Mathew. J. the facts were as follows : The assessee company was a foreign firm carrying on business, inter alia, in England in Guano, imported from South American into

England and sold there. Short loans were obtained from time to time from bankers to enable the company to pay more advantageously its purchase of cargoes of Guano. The question was whether interest paid on such loans could be considered, under the circumstances of the case, as revenue expenditure chargeable against profits, or whether it was expenditure of a capital nature. Viscount Cave said as follows :

It is contended by Mr. Finlay that in order to ascertain the balance of profits or gains of such trade you must taken into consideration the question whether the trader is trading with borrowed money, or with the capital of his own. It seems to me that that is not so - that the gains of the trade are quite independent of the question of how the capital money is found, that the gains of the trade are those which are made by legitimate trading after paying the necessary expenses which you have necessarily to incur in order to get the profits; and that you cannot for that purpose take into consideration the fact that the firm or traders has to borrow some portion of the money which is employed in the business."

The learned judge pointed out that such an argument might lead to extraordinary results. Suppose there was a firm of two partners, one of whom was a man of means able to put in capital whereas the other partner had to borrow money and to pay interest thereon. The learned judge did not think that it was either fair or lawful to consider the capital contributed by the latter partner as the sum brought in after making allowance for the interest paid on the borrowing. The whole of the money brought in must be treated as capital. The next decision which comes very near to the facts of this case is a Canadian decision, *Bennett & White Construction Co. Ltd. v. Minister of National Revenue*. The assessee company carried on business, as contractors. In the course of the business, various sums had to be borrowed from the bank, for which Joseph G. Bennett, one of the original incorporators and a large shareholders, stood guarantee for a consideration. After his death, his widow continued the guarantee and large sums were paid to both of them in consideration of their guarantee. The company obtained large war contracts and made extensive profits. The questions was whether the amount paid to Mr. Joseph G. Bennett and his widow was allowable as revenue expenditure. Rand J. said as follows :

"The acquisition of capital may be various methods including stock subscriptions, permanent borrowings through issues of securities, or term loans; and ordinarily it should make no difference in taxation whether a company carried on financially by one means or another. In the absence of statute it seems to be settled that to bring interest paid on temporary financing within deductible expenses requires that the financing be an integral part of the business carried on. That is clearly exemplified where the transactions are those of daily buying and selling of securities : *Farmer v. Scottish North American Trust* : or conversely lending money as part of a brewery business *Reids Brewery v. Male*.

Now the Crown has allowed the deduction of interest paid to the bank, and it must have been either on the footing that the day-to-day use of the funds was embraced within the business that produced the profit, or that the interest was within section 5, paragraph (b) But setting up that credit right or providing the banking facilities is quite another thing from paying interest; it is preparatory to earning the income and is no more part of the business carried on than would be the work involved in a bond issue.... Within the meaning of the Act, the premiums create part of the capital structure and are a capital payment : *Watney v. Musgrave*. They furnish a credit apparatus to enable the business to be carried on, and although they affect the distributable earnings of the company, they do not affect the net return from the "business."

Estey J. said as follows. :

"This was not a borrowing of money on a temporary or short-term basis sic as is necessary and incidental to the ordinary and usual transactions in the course of the appellants business. In effect, this line of credit made available to the appellant for an indefinite period the ability of borrows funds for the purpose of accepting contracts beyond the volume is paid-up capital and surplus would permit...

The appellants position is similar to that of a taxpayer in the *European Investment Trust Co. Ltd. v. Jackson*, where it was engaged in the business of financing the purchase of automobiles. Its paid-up capital was relatively small and the when that and the proceeds of a loan, admittedly capital, from the Finance Corporation of American, were exhausted, in order to finance further purchases it was arranged that the Finance Corporation of america would make further advances. It was contended that the interest on these further advances should be deducted in computing the profits. These advances were made as acquired by the taxpayer and were repaid by amounts as received from the purchasers. They were described by the taxpayer as short loans and the interest was computed upon monthly statements. The Commissioners found as a fact that the proceeds of these additional advances were employed or intended to be employed as capital in the trade and that, therefore, the interest paid could not be deducted in computing profits. On appeal this decision was affirmed. The taxpayer in that case, as the appellant here, when its capital was exhausted found it necessary to borrow in order that further contracts or a larger volume of business might be accepted... The appellant upon obtaining this line of credit was enabled to complete its financial arrangements at the bank, which enabled it to undertake the larger volume of business. Sums borrowed under such circumstances are capital and the sums paid are not deductible under the provisions of section 6(1)(a)."

The Supreme Court of Canada referred to a decision of the Privy Council - *Tata Hydro Electric Agencies Ltd. v. Commissioner of Income-tax*. In that case, the appellant company was said to have deducted from its profits, as expense, 25% of the annual commission earned by it, which it

had agreed to as part of the purchase price of the agency under which the amount became payable. Lord Macmillan said as follows :

"Their Lordships recognize, and the decided cases show, how difficult it is to discriminate between expenditure which is, and expenditure which is not, incurred solely for the purpose of earning profits or gains. In the present case, their Lordships have reached the conclusion that the payments in question were not expenditure so incurred by the appellants. They were certainly not made in the process of earning their profits; they were not payments to creditors for goods supplied or services rendered to the appellants in their business : they did not arise out of any transactions in the conduct of their business. That they had to make those payments no doubt affected the ultimate yield in money to them from their liability into that is not the statutory criterion. They must have taken this liability into account when they agreed to take over the business. In short the obligation to make these payments was undertaken by the appellants in consideration of their acquisition of the right and opportunity to earn profits, that is, of the right to conduct the business, and not for the purpose of producing profits in the conduct of the business. If the purchaser of a business undertakes to the vendor as one of the terms of the purchase that he will pay a sum annually to a third party, irrespective of whether the business yields any profits or not, it would be difficult to say that the annual payments were made solely for the purpose of earning the profits of the business."

It was held that on the facts of the commission paid was not revenue expenditure.

In a Bombay decision, the facts were very much like the present case, In re Tata Iron & Steel Co. Ltd. In that case, the Tata Iron & Steel Co. Ltd., a joint stock company, increased its capital by the issue of new shares for, which it paid about Rs. 28,00,000 as under-writing commission. It was held that this commission could not be allowed as an item of revenue expenditure. Macleod C.J. said as follows :

"Expenses incurred in raising capital are expenses of exactly the same character whether the capital is raised at the flotation of the company or thereafter : Texas Land & Mortgage Co. v. William Holtham. It was never suggested in that case that the expenses incurred in raising debentures were monies wholly or exclusively laid out or expended for the purpose of the trade, manufacture, adventure or concern of the company..."

A similar decision was arrived at by the Judicial Commissioner, Nagpur in Nagpur Electric Light & Power Co. Ltd. v. Commissioner of Income-tax. In that case, an electric light and power company raised a debenture loan of Rs. 6,00,000 on the security of its total assets. This was required for changing the system of supplying current from D.C. to A.C. and for discharging a prior loan. Certain moneys were paid as brokerage, registration and legal expenses. It was held

that these expenses were not allowable deduction in the company's assessable income. The learned judge relied on *Texas Land & Mortgage Co. v. William Holtham* and *In re Tata Iron & Steel Co. Ltd.* and came to the conclusion that the expenditure was not allowable because they were of the nature of capital expenditure. In *London Country Freehold & Leasehold Properties Ltd. v. Sweet* the facts were as follows : The appellant company was an investment company deriving its income from rents received from freehold and leasehold properties. During the years 1933-38, it issued new debentures and stocks for the purposes of repaying the existing debentures, specific mortgages, bank loans and other charges. Certain expenses were incurred for the issue of the new debenture stock and were claimed as allowable deduction. It was held that such expense could not be allowed. It was argued that these were expenses not in raising the original capital but in re-arranging the loan capital in a manner more satisfactory to the company. It was held that nevertheless this was a more satisfactory one to the company. It was held that nevertheless this was a capital expenditure and not an allowable deduction. In *Ascot Gas Water Heaters Ltd. v. Duff* the appellant company raised a first mortgage debenture stock for extension of its business. For this purpose a Dutch company gave a guarantee and charged from the appellant, a commission. It was held that the commission was not an allowable expenditure.

Lawrence J. pointed out that if the sums in respect of which deduction was claimed were temporary in their nature and might be regarded as an ordinary expenditure of carrying on the business of the company, they could be allowed, but expenditure for raising mortgage debenture capital could not be considered as a temporary accommodation. It may be noted that in this case it does not appear that there was no limit as to the time for repayment of the debt and also there was no limit to time for which the guarantee was given and the commission paid thereon. In the case of *Western India Plywood Ltd. v. Commissioner of Income-tax the Kerala High Court* has laid down the correct principle. The facts in that case were as follows : The assessee was a public limited company carrying on business as manufacturers of plywood articles. It raised a loan of Rs. 3 lakhs by way of first mortgage debentures, redeemable in three successive years at the rate of Rs. 1 lakh every year. Part of the money was borrowed for the purchase of timber and casein, part for cash purchase, part for discharging loans on suspense account and the remainder was deposited in a separate account for payment of dividends. In issuing the debenture, the company incurred Rs. 12,924 by way of expenses towards the purchase of stamp paper for the trust deed, underwriting commission and registration and lawyers fees. The question was whether this sum could be allowed as business expenditure and was deductible under section 10(2)(xv) of the Income-tax Act, Pillai J. said as follows :

"On the arguments addressed to us, the only question which arises for decision is, whether the sum of Rs. 12,924 is in the nature of a capital expenditure. As a first step of debenture to the extent of three lakhs of rupees. If the amount so raised is capital receipt, money expended to raise it has

to be held to be in the nature of capital expenditure, either as forming part of the capital so raised and reducing the amount available to the assessee pro tanto or alternatively, as partaking of the same character as such capital itself. The question therefore resolved itself the sum of three lakhs of rupees raised by debenture is a capital receipt or a revenue receipt. Though the term capital expenditure is not defined in the Act, as observed by Shah J in *In re Tata Iron & Steel Co. Ltd.* the words in the nature of capital expenditure make the meaning of the expression elastic in its application to the facts of each case. Capital may be subscribed or borrowed and as for the latter, the Act itself makes allowance for interest payable in respect of it. A borrowing of capital has to be distinguished from securing *à mere* temporary or day-to-day accommodation, or from, banking or overdraft facilities, and may be either by way of addition to the capital or for improving the capital position. The above distinction was pointed out by Finlay J. in *Eruopean Investment Trust Co. Ltd. v. Jackson* and was affirmed by Lawrence J. in *Ascot Gas Water Heaters Ltd. v. Duff*, who considered a temporary accommodation to be an ordinary incident in carrying on the business. In a commercial sense, no one would speak of his banking facilities as part of his capital assets. In *Ward v. Anglo Americal Oil Co. Ltd.* Singleton J. quoted as follows from the judgment of the court of Sessions in *Scottish North American Trust v. Farmer*.

It may well be said that if money is borrowed on a permanent footing, as from year to year, the capital of the concern is in commercial sense enlarged thereby, and the business extended....

The category of short loans which may be contracted in carrying on a business also comes within the scope of temporary accommodation or of ordinary trading facilities. But the raising of the money by debentures or mortgage cannot be regarded as an ordinary incident in carrying on the business, or be treated as on a par with trading or banking facilities, but must *prima facie* and in the absence of other indications be considered to affect the capital of the concern and its profit-making structure."

It was argued that the borrowed money represents circulating capital as distinct from fixed capital and, therefore, borrowing on debenture should not be put on a different footing. The learned judge however said as follows :

"Viscount Haldane, in *John Smith & Son v. Moore*, has adopted Adam Smiths definition of fixed capital as what the owner turns to profit by keeping it in his own possession, and of circulating capital as what he makes profit of by parting with it, and letting it change master. The term circulating capital has thus been used as synonymous with the term stock-in-trade or the term trading assets, as distinguished from fixed capital or capital assets. What is fixed capital for one business or trade may be circulating capital for another, depending on the nature of the business or trade..... At one stage of the argument, counsel seemed to assume that the enlargement or extension of business can only be in additional building, plant or machinery; we do not see

sufficient warrant for this assumption, though cases of additional business are conceivable without a corresponding addition to capital. It is clear law, that outlay for the extension of business is in the nature of capital investment..."

Before us Mr. Mitter has argued that we should not place reliance on English decisions as they turn on the wording of the English statute. The very same argument was advanced before the Kerala High Court, but the learned judges stated as follows :

"The learned counsel for the assessee cautioned us against accepting too readily the decisions of the English courts, as they are based on different statutory provisions. We agree that the provisions of the concerned statutes in England and in this country are not all in pari materia, but in the study and elucidation of fundamental concepts and general principles, like capital receipts and disbursements, revenue receipts and disbursements as pointed out by the Supreme Court itself in Commissioner of Income-tax v. Vazir Sultan & Sons English decisions afford considerable help and guidance. Before advertng to them, it has to be borne in mind, that under the English statutes too, from 5 and 6 Vict. c. 35 down to 15 and 16 Geo. 6 and 1 Eliz. 2 c 10 (being the Income Tax Act, 1952), questions do arise as to the nature of the receipt, whether capital or revenue, as no deduction is permissible in respect of any capital withdrawn form or any sum employed or intended to be employed as capital in a trade, profession or vocation."

It had also been strenuously contended before us that a payment, like a percentage on the gross receipts for an indefinite period cannot be in the nature of capital. Reference may be made to National Cement Mines Industries Ltd. v. Commissioner of Income-tax. There, the assessee company acquired certain rights and concession pertaining to limestone and other mineral substances necessarily for manufacturing cement, and transferred the same to another company which, inter alia, agreed to pay a sum of 13 as for every ton of cement sold by it. There was no limitation as to period. The question was whether such a payment was a capital or revenue expenditure. Chakravarti C.J. said as follows :

"... it will not be correct to adopt any single test as a test of universal application and it will be well to remember the observations of Lord Greene M. R. in the case of Commissioner of Inland Revenue v. 36/49 Holdings Ltd :

The true nature of the sum is not necessarily its nature in law, but its nature in business or in accountancy, whichever way one likes to put it, because from the legal point of view, there may be no difference whatsoever as between the parties between a capital and an income sum. It may be totally irrelevant to the legal relationships into which they are proposing to enter. When, however, the tertius gaudens, in the shape of the revenue, appears on the scene, that matter which as between the parties, may have been a matter of not the slightest importance, becomes

immediately a matter of very great importance, and it is necessary to examine the circumstances of each individual case, including any documents which require to be construed, in order to ascertain what is the character to be attributed to the payment. That is why, I say that I personally find very little assistance from examining the circumstances of other cases...

"On the facts of the case, however, the learned Chief Justice decided that the amount paid was in the nature of capital receipt.

Mr. Meyer has next taken us to the provisions of the companies Act, 1956, for the purposes of showing what "capital" means and whether the issue of debentures amounts to the acquisition of capital. The word "capital" is not defined either in the English or the Indian Act. The expression "share capital" has however been used and in Part IV of the Indian Companies Act share capital and debentures have been dealt with together and may be taken to be of a similar nature. In Part III, also the issue of shares and debentures are dealt with together. The word "debenture" is defined in section 2(12) and includes bonds. Section 157 also equates share capital and debentures. The matter has been clearly explained in Halsburys Laws of England, third edition, volume 6, at page 18. Under the heading "capital of the company" It has been explained that there may be different kinds of capital, namely, "authorised capital" "subscribed capital" as well as "loan capital". Where a company is authorised to raise capital by way of loan it may issue debentures or debenture stock or mortgages or bonds, and these are its "loan capital". It appears, therefore, that the raising of capital by the issue of debentures is a recognised mode.

Mr. Meyer has rightly pointed out that all the decided cases have laid down the proposition that borrowings money by the issue of debentures is an acquisition of capital assets and that any commission or expenditure incurred in respect thereof is of a capital nature and not to be considered as in the nature of revenue. There is significantly not a single case to the contrary. Mr. Mitter appearing on behalf of the assessee has not seriously argued that the issue of debentures is not an usual method of acquiring capital. He argues, however, that, on the facts and circumstances of the present case, a payment of commission to a broker for raising a loan a payment which was going to be made irrespective of profit and made for perpetuity, should not be considered as an expenditure is of a capital nature. Doubtlessly, as pointed out by Chakravarti C.J., the determination of whether a particular expenditure is of a capital nature or revenue nature depends on the facts of each case. The mere fact, however, that it has to be paid irrespective of profits or for a large number of years (see *Delage v. Nugget*) or indefinitely (see *Bennett & White Construction Co, Ltd. v. Minister of National Revenue*) does not render it any the less a capital expenditure. Mr. Mitter next tried to argue the case on general principle. For example, he has cited the case of *British Insulated & Helsby Cables Ltd. v. Atherton*, which is the leading case on the question of capital and revenue expenditure. Viscount Cave laid down the following

test :

"But 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 a trade, I think that there is very good reason (in the absence of special circumstances leading to an opposite conclusion) for treating such an expenditure as properly attributable not to revenue but to capital."

Viscount Caves proposition is an amplification of a proposition laid down earlier by Lord Dunedin in the case of *Vallambrosa Rubber Co. v. Framer* where he held that normally an expenditure made once and for all would be capital expenditure and expenditure which would be recovered year after year would be an expenditure on revenue account. Chakravarti C.J. in *Royal Calcutta Turf Club v. Commissioner of Income-tax* has explained that the test of the expenditure being made once and for all would not always suffice to mark out a particular item of expenditure as expenditure of a capital nature. It is true that the learned Chief Justice held that the expenditure with which he was concerned was not a capital expenditure for the reason that it was not an expenditure made once and for all; but it also depended on the facts of that particular case. The assessee in that case was the Royal Calcutta Turf club. Some time before 1948, the said club came to think that there was a risk of a serious decline in the number of jockeys available in Calcutta and took steps to establish a school for training Indian boys as jockeys. The experiment was, however, unsuccessful and was given up after a brief existence. The question was, whether the expenditure incurred in connection with the school was a capital or revenue expenditure. The learned Chief Justice said as follows :

"The assessee club had founded and was running a school for the purpose of safeguarding its business interests and the expenditure was only a years portion of the recurring expenditure that was being incurred year after year for the maintenance of the school. It was not as if the assessee had spent a single and definite sum either in a lump or in instalments for the purpose of securing an assets or an advantages, even assuming that an asset or an advantage was intended to be secured. The expenditure being only the running expense of keeping the school, was of the nature of expenditure which is incurred for meeting a continuous demand in connection with ones business. Even judged by the First part of Viscount Caves test, it appears to me, the expenditure with which we are concerned cannot be said to have been a capital expenditure."

The rest of a single expenditure is however only one of the tests and cannot be of universal application.

Another case relied on by Mr. Mitter is a decision of the Supreme Court Dharamvir Dhir v. Commissioner of Income-tax. In that case, the assessee was an employees of a firm earning into a coal a salary of Rs. 10,572 and Rs. 500 from shares annually. He entered into a coal raising

contract with a coal company which involved several lakhs of rupees. But as he did not have the requisite funds for the business, he entered into, an agreement with a public charitable trust for advancing moneys on every stringent terms. This included an interest of 6 percent. and 11/16th of the profits of the business. During the assessment years, the assessee had to pay large sums to the trust, which in its advanced several lakhs of rupees. The question was whether these sums were allowable as revenue expenditure. It was held by the Supreme Court that, on the facts of that particular case, and taking into account all the surroundings circumstances, it was an allowable, expenditure and not of a capital nature. It was pointed out that the trust was lending large sums of moneys without any security, upon a venture which might not have been successful, and the reasonable conclusion was that the amount was expended as a matter of commercial expediency and for the purpose of earning profits and was, therefore, a deductible expenditure. The case of Pondicherry Railway Co. Ltd. v. Commissioner of Income-tax was distinguished on the ground that in the said case, the assessee company which obtained a concession for èconstructing railway in the territory of Pondicherry agreed to pay to the French Government half of its net profits. It was held by the Privy Council that the payment could not be of a revenue nature, because it was conditional upon profits coming into existence. As soon as the profits came into existence, it attracted taxation at that point and the revenue was not concerned with the subsequent application of the profits. In the present case, the payment is not conditional upon profits. It was pointed out that what was money wholly and exclusively laid out for the purposes of the trade was a question which must be determined upon the principles of the trade was a question which must be determined upon the principles of ordinary commercial trading. It was necessary, accordingly, to attend to the true nature of the expenditure, and to ask oneself the question was it a part of the companys working expenses ? Was it expenditure laid out as part of the process of profit-earning ? Thus in Commissioner of Income-tax v. Tata Sons Ltd, the company received a commission on the basis of profits. The managed company was in urgent need of money and the assessee company found a financier, a Mr. Dinshaw, and an agreement was entered into with the managed company and Mr. Dinshaw by which the latter agreed to lend a crore of rupees on the condition that the assessee company assigned to him a share in the commission which the assessee company might receive from the managed company. That was held to be an agreement on the part of the assessee company to share their commission with Mr. Dinshaw and it was a part of the arrangement on which the assessee company obtained finance and therefore, the payment to Mr. Dinshaw was an expenditure solely for the purpose of earning profits or gains and it was not of a capital nature. Beaumont C.J. said that the question whether the payment of a part of the commission to a third person should be regarded as expenditure incurred solely for the purpose of earning that commission was a question which must be answered on the facts of each case and upon a commercial basis. I must confess that the cases on this aspect of the question are not always reconcilable. It is however clear that the

commission paid on the issue of debentures upon the security of the company's assets has always been considered as in the nature of capital expenditure and not in the nature of revenue expenditure.

For the reasons aforesaid, I am of the opinion that the commission agreed to be paid to certain persons in consideration of the raising of a loan by the issue of debentures by the assessee company is to be considered, in the facts and circumstances of this case, as in the nature of capital expenditure and not in the nature of revenue expenditure, which would make it a deductible expenditure under section 10(2)(xv) of the Income-tax Act. In my opinion, the question asked should be answered in the affirmative.

DATTA J. - This reference arises in these circumstances :

On or about the 26th January, 1950, the assessee company raised a loan of Rs. 10,00,000 by issuing debentures redeemable in ten annual instalments of Rs. 1,00,000 each commencing from 31st December, 1954. On the same day the company agreed to pay to one Jogendralal Nandy and Anil Krishna Paul a commission at the rate of one per cent. in perpetuity, that is, for even on the gross sale of the products of the company in consideration of their securing the said debenture loan of Rs. 10,00,000.

On the 17th June, 1950, Jogendralal Nandy died. Thereafter on the 10th December, 1951, the heirs and legal representatives of Jogendralal Nandy and Anil Krishna Paul assigned their right to receive the commission in perpetuity to one Sunil Kumar Paul and Amal Krishna Poddar. In the assessment year 1952-53, corresponding to the accounting year, being the calendar year 1951, the company paid a sum of Rs. 21,798 to the said Sunil Krishna Paul and Amal Krishna Poddar. The assessee claimed the said sum of Rs. 21,798 as an admissible expenditure under the residency clause of section 10(2), sub-clause (xv).

The Income-tax Officer and the Appellate Assistant Commissioner disallowed the claim of the assessee "on the ground that the expenditure was of a capital nature". The Appellate Tribunal repelled the contention advanced on behalf of the assessee that the company by assuming debentures acquired a liability and not an asset of an enduring character and held, inter alia, as follows :

Although, as a matter of fact, the loan was a liability in the sense that it had to be repaid, the sum secured by the loan became a part of the assets of the company. The loan was not a short-term one being redeemable in instalments by the end of December, 1963. The Tribunal was of the opinion that the loan of Rs. 10,00,000 raised by the company conferred on it the benefit of enduring character and it was, therefore, a capital asset in the hands of the company. An

expenditure incurred for securing capital must be regarded that the amount of Rs. 21,798 which was paid by the company was of the nature of capital expenditure and, consequently, no deduction could be allowed under section 10(2) (xv)."

Thereafter the Tribunal referred the following question of law to the High Court :

"Whether, on the facts and in the circumstances of the case, the sum of Rs. 21,798 was a capital expenditure and, as such, not allowable as a deduction under section 10(2)(xv) of the Indian Income-tax Act ?

The provision of section 10(1) are as follows :

"The tax shall be payable by an assessee under the head "profits and gains of business, profession or vocation" in respect of the profits or gains of any business profession or vocation carried on by him."

The relevant provisions of section 10(2) is as follows :

Such profits or gains shall be computed after making the following allowances namely :....

(xv) Any expenditure (not being allowance of the nature described in any of the clauses (1) to (xiv) inclusive, and not being in the nature of capital expenditure or personal expenses of the assessee) laid out or expended wholly or exclusively for the purpose of such business, profession or vocation."

Sub-clauses (1) to (xiv) of clause (2) of section 10 enumerate the specific heads in respect of which deductions are allowed.

Sub-clause (xv) of clause (2) of section 10, however, does not enumerate any specific head but is a residuary head circumscribed by certain limits.

Sub-clause (xv) or the residuary sub-clause is attracted when three conditions are satisfied :

- (1) An expenditure not being an allowance of the nature described in any of the clauses (1) to (xiv) inclusive.
- (2) Not being in the nature of capital expenditure or personal expenses of the assessee.
- (3) Laid out or expended wholly or exclusively for the purpose of such business, profession or vocation.

In the discussion before us the matter proceeded more often on the basis that the assessee in

order to succeed in the reference must fulfil two conditions : firstly, that the commission was not in the nature of capital expenditure and, secondly, that the commission was laid out or expended wholly or exclusively for the purpose of such business or profession or vocation.

Hence it would not be sufficient if the commission paid was not in the nature of capital expenditure but it must also be an expenditure laid out or expended wholly and exclusively for the purpose of such business. On the other hand it would not be sufficient if it is found that the expenditure was laid out or expended wholly and exclusively for the purpose of such business but it would be necessary to further establish that the expenditure was not in the nature of a capital expenditure. Therefore, one way of approaching the problem is to determine, firstly, whether the expenditure is in the nature of a capital expenditure. If it is so, then to determine whether the expenditure was laid out or expended wholly and exclusively in the nature of a capital expenditure, then it would be unnecessary to investigate whether the expenditure was laid out or expended wholly and exclusively for the purpose of such business.

There can be another approach to the same problem.

It may be determined first whether the expenditure was laid out or expended wholly and exclusively for the purpose of such business. If it was so, then to investigate the next clause whether it was in the nature of a capital expenditure. If it be found that the expenditure was not laid out or expended wholly and exclusively for the purpose of such business, it would be unnecessary to find out whether the expenses were in the nature of a capital expenditure.

In my view having regard to the limited nature of the question, the first way of approach to the problem would be more convenient in this case. In other words, we will first consider whether the sum of Rs. 21,798 was in the nature of a capital expenditure and then consider if the expense was not in the nature of a capital expenditure, whether the said expenditure was laid out or extended wholly or exclusively for the purpose of the business, profession or vocation.

"capital" has different meanings.

Capital comprises ordinarily, from a commercial mans point of view, not only the moneys raised by the issue or sale of shares but also moneys raised by way of loans either by the issue of debentures or otherwise. It is not this capital in the phrase "in the nature of capital" that sub-clause (xv) has in view, for it does not deal with the origin or source of capital raised but deals with expenses incurred or moneys spent out of capital however raised.

The capital raised by the issue of shares or by way of loans is meant to be spent on different items with a view to earn profit. It may be utilised for the purchase of plant, machinery, land for building factories and so forth which are capital goods. It may again be utilised or spent in

paying ordinary expenses for running the business such as rent, electric charges, salaries, wages and/or in the purchase of stock-in-trade. Therefore the expenditure may be made in the two categories of things or matters. The first is known as expenses in the nature of capital expenditure. The second is known as revenue expenditure. Capital in this sense is opposed to revenue expenditure.

It is the capital or expenditure in the nature of capital as opposed to revenue expenditure to which sub-clause (xv) of clause (2) of section 10 of the Income-tax Act is directed against.

The expenses in the nature of capital expenditure arise only when moneys however raised or capital is spent and not before. So its quality as capital expenditure or revenue expenditure comes into existence and/or is determined by the nature of the expenditure whether it is invested in capital goods and intangible things which partake the nature of capital goods or not. To put it differently, the quality or attribute of the capital howsoever raised, when in the control or possession of the company before it is spent, cannot determine the nature or quality of the expenditure.

Therefore, in my opinion, the expenditure by way of commission should be considered on its own merit as an expenditure divorced from the nature of its origin, that is to say, the source of the capital raised. If the commission paid for the loan raised is considered independently, then it is not possible to say that it is a capital expenditure or in the nature of a capital expenditure for the commission itself does not find its way or is not translated in any capital goods or any intangible thing which is in the nature of capital goods which can reproduce wealth or be the instrument or medium of earning profit but is spent and gone. Hence commission paid cannot be a capital expenditure and must be a revenue expenditure.

It is now necessary to turn to some of the authoritative pronouncements on the point of expenditure or expenditure in the nature of capital expenditure.

Lord Dunedin in *Vallambrosa Rubber Company v. Framer* laid out a test in these words :

"Capital expenditure is a thing that is going to be spent once and for all. An income expenditure is a thing which is going to recur every year."

Lord Atkinson suggested that in *British Insulated & Helsby Cables Ltd. v. Atherton* the word "asset" ought not to be confined to something material, for it may be an advantage of man impalpable or incalculable nature or it has been said it may be an expenditure which increases the value of the capital asset. In the facts of *British Insulated & Helsby Cables Ltd. v. Atherton* the test laid down by Lord Dunedin could not be applied.

Viscount Cave L.C. in the course of his speech in *British Insulated & Helsby Cables Ltd. v. Atherton* said as follows :

".... 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 a trade.... there is very good reason (in the absence of special circumstances leading to an opposite conclusion) for treating such an expenditure as properly attributable not to revenue but to capital."

In *Anglo Persian Oil Co. Ltd. v. Dale* Lord Justice Romer explained the meaning of "enduring" He said "enduring " means enduring in the way that fixed capital endures."

Lord Justice Romer further said that any expenditure with a view to the bringing an asset or advantage into existence should be stamped as capital expenditure.

Bhagwati J. observed in *Assam Bengal Cement Co. Ltd. v. Commissioner of Income-tax* that the expression "once and for all" used by Viscount Cave L.C. does not mean that the payment should be made in a single sum and at one time, for the expression "once and for all" is used to denote an expenditure which is made once and for all of procuring an enduring benefit to the business as distinguished from a recurring expenditure in the nature of operational expenses.

The underlying principle to my mind is the definition of capital by Adam Smith. That concept has been fashioned and chiseled by judicial pronouncements to suit the facts of a particular case in what are known as borderline cases. The borderline cases, present more difficulty when expenditure in the nature of capital expenditure is incurred in more or less intangible things as opposed to capital goods.

In my opinion, the essential features of the tests laid in the above cases fortify the conclusion to which I have arrived at, namely that the commission or brokerage paid for raising loan capital cannot be an expenditure in the nature of a capital expenditure.

There are several decisions of the English courts which militate against the conclusion that the commission payable for raising capital is a revenue expenditure.

In *Arizona Copper v. Smiles* the question arose in this form : The Arizona Copper Co. borrowed money to be employed in its business and covenanted to pay only interest thereon and repay capital with an additional bonus of 10 per cent. The court held that the bonus cannot be claimed as a deduction in estimating the assessable profits of the company. The Lord President discussed the matter as follows :

"The question before the court is whether the Arizona Copper Company, the borrowers, are

entitled to deduct this bonus in returning their profits under the Income-Tax Acts.

There cannot be said to be any complexity or ambiguity in the application of the money or in the source from which it was paid. It was paid in a lump payment as one of the considerations stipulated for a loan of capital employed in the completion of the works, the other consideration being interest at 10 per cent. per annum and it is in terms admitted in the case to have been paid out of the profits of the company. Now at this stage of the development of the law of the profits of the Income-tax it is not to the purpose to consider whether such a payment is a proper deduction, from the point of view of a business concern, making up its own balance sheet for its own purposes. The question is whether such a payment out of thereof is an authorised deduction in estimating the balance chargeable under Schedule D. It appears to me, as a sum paid in return for a loan of which is permitted as being necessarily incidental to the earning of profit and I think to deduct it would be contrary to the prohibitions laid down in Schedule D and in the 159th section of the same Act."

In *Texas Land & Mortgage Co. v. Holtham*, a company raised money by the issue of debentures and lent it at a higher rate of interest. It was held that the commission paid to the brokers, and the other expenses incurred in raising the money, cannot be deducted under Schedule D as trade expenses. Mr. Justice Mathew delivering his judgment dealt with the matter as follows :

"To increase its capital it raised money on debentures. The argument is that the cost of raising the money ought to be deducted from the profits in a particular year. We are clearly of opinion that that cannot be done. The amount paid in order to raise the money on debentures, comes off the amount advanced upon the debentures, and, therefore, is so much paid for the cost of getting it, but there cannot be one law for a company having sufficient money to carry on all its operations and another which is content to pay for the accommodation."

These are some of the leading cases which have established the rule in England that commission payable for raising capital is a capital expenditure.

In India the *Texas* case was followed by the Bombay High Court where the problem was whether commission paid to underwriters of the shares of the assessee company was an item of expenditure under section 9. clause (2), sub-clause (ix) of the Income Tax (7 of 1918). The *Texas* case was again followed in India by the Judicial Commissioners, Nagpur, in *Nagpur Electric, Light and Power Co. Ltd. v. Commissioner of Income-tax*, where it was held that sums of money paid as brokerage, registration and legal expenses for raising the loan are not allowable as deduction in the computation of the company's assessable income."

The decision in *Arizona Copper Co.* case was founded on the construction of sub-clause (f) of

rule 3 of Schedule D of English Act which provided that "In computing the amount of the profits or gains to be charged, no sum shall be deducted in respect of any capital withdrawn from or any sum employed or intended to be employed as capital in such trade, profession or vocation". The scheme of the English Act is different from the scheme of the Indian Income-tax Act. Moreover, in the English Act there is clear provision in sub-clause (f) regarding payment of money out of the capital whether it be share capital or loan capital. There is no similar provision in our statute. Hence the principle deduced from the English Act cannot be applicable without close scrutiny of the Indian Income-tax Act. The Taxes case was likewise founded on sub-clause (f) of rule 3 for it is stated in the judgment that "the amount paid in order to raise the money on debentures comes off the amount paid in order to raise the money on debentures comes off the amount advanced upon the debentures." In India the test is not whether it is the expenditure by way of commission that falls within sub-clause (f) of rule 3 but test is, as we have seen earlier, whether it is a capital expenditure or not and if it is not capital expenditure, whether it was laid out exclusively for the purpose of the business. In my opinion, the decision in 3 Taxes Cases are well-founded on the basis of the English Act. They have however no application whatsoever, in India where both the schemes and the words are different. Hence in my opinion, the reasoning mentioned therein cannot be applicable to the same problem in India.

In this view of the matter, in my opinion, the English cases and the Indian cases offer no impediment to the conclusion to which I have arrived at.

In the course of then arguments another series of cases were referred to where it was held that interest paid for raising borrowed capital is capital expenditure when it is borrowed for a long term and is a revenue expenditure when borrowed for short period. The decisions again in these cases were influenced in England by the proviso of clause (f) of rule 3 of Schedule D. Here again the character to quality of the raised capital is applied to test whether the interest is a capital expenditure or not.

In my opinion whereas in India we are not fettered as in England, the test should be different from that which has been laid down in these English cases.

In England again the rule laid down in Taxes case has been followed in all circumstances.

In commissioner of Inland Revenue 36/49 Holdings Ltd. the problem was whether a commission payable in perpetuity on the basis of the out-term of company was in the nature of a capital expenditure or revenue expenditure. It was observed by Lord Greene that case turns on its own facts and the presence or absence of one factor may tilt the balance either way. His Lordships held that, as the commission was payable in perpetuity, was related to turnover and was not tied in any way to any special sum, it could not be an expenditure in the nature of a capital

expenditure but a revenue expenditure.

It may be observed that ratio decidendi of the Taxes case was not applied to the facts of that case, for the commission payable was not withdrawn from any capital and raised or any particular fund employed in the capital of the business.

In *Delage v. Nuggett Polish Co. Ltd.* the question came again for consideration. There the facts were, as correctly summarised in the headnote as follows :

"By an agreement between the plaintiffs and the defendant, the defendants had exclusive right of selling and manufacturing articles by a secret process and the defendants were to pay to the plaintiffs for 40 years 8s. per cent on the gross receipts of such sale. The plaintiffs resided abroad and were foreigners and before paying the amount payable to them under the agreement, the defendants deducted income-tax in respect of the amount due under the agreement."

In these circumstances, the court held that the income-tax was rightly deducted. This case again can be distinguished from the Texas case on the ground that it was not withdrawn from the capital or was not tied to a specific fund.

In India Chief Justice Chagla and Mr. Justice Tendolkar in *Commissioner of Income-tax v. Kolhia Hirdagarh Co. Ltd.* held that a payment of an annual dividend of four annas for every ton of coal from the colliery of the assessee company was a payment made for an indefinite period. The payment made in relation to the turnover of the company and not in relation to its profits and as the profits had no bearing to any specific fixed sum for the purchase of the undertaking, it was in the nature of revenue payment and not a capital payment.

Therefore, in my opinion, even the principle of the Texas case founded on sub-clause (f) of rule 3 of Schedule D of the English Act could not have any application in a case where the commission is payable in perpetuity.

The provision for payment of commission in the case before us may now be examined and then considered in the light of the judicial pronouncements adverted to earlier.

In this case the obligation to make this annual payment every year was in perpetuity for the loan capital raised by the company. It is a fluctuating amount not depending on the capital raised. It is not a fixed amount which has to be paid every year.

It is payable even when loss is incurred. It is payable so long as there is any sale. It does not depend on the profits or loss. It depends on the sale. It does not end with repayment of the loan, but it continues in perpetuity so long as there is a sale of its products. It is not associated with

the capital raised but with all capital outlay as long as the mill continues to manufacture its finished goods. It may be an unlimited sum of money which may exceed the loan raised by a number of times. It may or may not be paid out of the capital raised or even from all capital assets.

Hence these payments do to fall within the rules laid down by authorities England to determine capital expenditure to expenditure in the nature of capital expenditure. The expenditure of Rs. 21,798 is not an expenditure which is invested in the means of production or capital. The expenditure Rs. 21,798 dissociated from the capital raised or its origins not an expenditure which brings enduring benefit. The commission is not paid once and for all. The expenditure of Rs. 21,798 is not invested in circulating capital. Hence in my opinion it does not attract any of the tests laid down for determining a capital expenditure or an expenditure in the nature of a capital expenditure.

Hence, again, in my opinion, the commission paid was a revenue expenditure.

The question as framed is in a limited form. It is directed only against the element of expenditure in the nature of capital. It is silent as to the question whether it was laid out or expended wholly and exclusively for the purpose of business. In other words, the question assumes that the expenditure was laid out or expended wholly and exclusively for the purpose of business. In other words, the question assumes that the expenditure was laid out or expended wholly and exclusively for the purpose of business.

Hence, in my opinion, the above conclusion that the commission paid was a revenue expenditure is sufficient to dispose of the matter before us and answer the reference in favour of the assessee.

In view of the facts that the question whether the sum of Rs. 21,798 was "laid out or expended wholly and exclusively for the purpose of business" was often treated as implicit in the questions before us and the same was agitated by both parties at considerable length, it is preferable to deal with this aspect of the matter and record my opinion thereon.

The words "laid out or expended wholly and exclusively for the purpose of such business, profession or vocation" and/or similar phrases have been the subject-matter of several decisions both in England and in India.

The case of *Pondicherry Railway Co. v. Commissioner of Income-tax*, may be referred to in this connection.

There the assessee company obtained a licence for constructing a railway in Pondicherry and in consideration thereof the assessee company undertook to pay half of its net profits to the French

Government. The assessee company contended that half of its net profits payable to the French Government was an allowable deduction under the provisions corresponding to section 10(2) (xv). Lord Macmillan repelled the contention of the assessee company for the reasons which are given in his own words :

"A payment out of profits and conditional on profits being earned cannot accurately be described as a payment made to earn profits. It assumes that profits have first come into existence. But profits on their coming into existence attract tax at that point and the revenue is not concerned with the subsequent application of the profits."

The observations of Lord Macmillan were often misunderstood and misapplied. Lord Macmillan therefore took the opportunity of explaining his view in *Union Cold Storage Co. Ltd. v. Adamson*. He observed as follows We were reminded very properly by the Solicitor-General that these cases all turn upon their particular circumstances, and in that case (*Pondicherry Railway Co. Ltd v. Commissioner of Income-tax*) the convention under which the payments were made provided as follows : the company undertakes on its part to make over to the colonial Government during the whole duration of the concession one-half of the net profits which shall be arrived at in a manner which is then set out in detail provision being made for the deduction of all outgoing, such as rates and taxes, and so on. In that case, therefore, the ascertaining, of profits preceded the coming into operation of the obligation to pay, and when the profits had been ascertained the obligation was to make over one-half thereof to the French Colonial Government. The obligation was conceived in language entirely different from the language which your Lordships have been considering in the present appeal, where there is a common firm obligation in a lease to pay rent. When , therefore, in the passage referred to by the Attorney-General in the *Pondicherry* case I said that a payment out of profits and conditional on profits being earned cannot be described as a payment made to earn profits, I was dealing with a case in which the obligation was, first of all, to ascertain the profits in a prescribed manner, after providing for all outlays incurred in earning them, and to divide them. Here the question is whether or not a deduction for rent has to be made in ascertaining the profits, and the question for rent has to be made in ascertaining the profits, and the question is not one of the distribution of profits at all."

In *Tata Hydro-Electric Agencies Ltd. v. Commissioner of Income-tax*, the assessee undertook to pay a quarter per cent. of the commission earned by it from *Tata Power Co.* independent of whether the assessee made any profit or not. There Lord Macmillan observed that the rule laid down in *Pondicherry Railway Co. v. Commissioner of Income-tax* did not apply. In the course of the judgment Lord Macmillan observed as follows :

In short the obligation to make these payments was undertaken by the appellants in consideration of their acquisition of the right and opportunity to earn profits, that is, of the right to conduct the

business, and not for the purpose of producing profits in the conduct of the business.

In *Commissioner of Income-tax v. Tata Sons Ltd.* similar problem came for decision. In that case where the managed company was in real need of money and the assessee company found a financier, a Mr. Dinshaw, and an agreement was entered into between the assessee company, the managed company and Mr. Dinshaw by which the latter agreed to lend a crore of rupees on condition that the assessee company assigned to him a share in the commission which the assessee company might receive from the managed company. In that case it was held that it was an allowable deduction of for it was incurred solely for the purpose of earning that commission.

In *Indian Radio & Cable Communications Co. Ltd. v. Commissioner of Income-tax* the observations of Lord Macmillan were further watered down when their Lordships observed that "it was not universally true to say that a payment the making of which is conditional on profits being earned cannot properly be described as an expenditure incurred for the purpose of earning such profits."

In *British Sugar Manufacturers v. Harris* where the assessee company agreed to pay to other companies a certain percentage of its annual profits after deduction of expenses and debenture interest "in consideration of their giving to the assessee company the full benefit of their technical and financial knowledge and experience." There it was held by the learned Master of the Rolls that such payments were in the facts of that case an allowable deduction.

In *Robert Addie and Sons Collieries Ltd. v. Commissioner of Inland Revenue* the Lord President sought to lay down the positive rule in these words :

"What is money wholly and exclusively laid out for the purposes of the trade is a question which must be determined upon the principles of ordinary commercial trading. It is necessary accordingly to attend to the true nature of the expenditure, and to ask ones self the question, is it a part of the companys working expenses ? Is it expenditure laid out as part of the process of profit earning ?"

In *Commissioner of Income-tax v. Chandulal Keshavlal & Co.* their Lordships of the Supreme Court, after discussing several decisions on this analogous problem, followed more or less the rule laid down in Addies case. The ground of the decision is summarised at page 611 as follows :

Thus in cases like the present one in order to justify deduction the sum must be given up for reasons of commercial expediency; it may be voluntary, but so long as it is incurred for the assessees benefit, the deduction would be climbable."

In *Dharamvir Dhir v. Commissioner of Income-tax* the Supreme Court had a further occasion to

discuss the meaning of the words "laid out or expended wholly and exclusively for the purpose of business". In that case an employee of Messrs. Karamchand Thapper & Brothers carried on business on his own account. He entered into a trade with the Bengal Nagpur Coal Co. Ltd. for arising coal for one of its mines. He did not have the necessary funds. So he entered into an agreement with Mohini Thapper Charitable Trust to obtain the necessary finance. The Trust agreed to advance Rs. 1 1/2 lakhs in consideration of the assessee paying interest at the rate of six percent per annum on the amount from time to time owing to the trust and in addition agreed to pay a sum equal to 11/16th of the net profits of the business of the assessee. It was found as a fact that on the average the trust estate advanced Rs. 1,97,000 to Rs. 17,000 and the assessee paid Rs. 72,963 as 11/16th part of the profits. In that case his Lordships discussed the cases of Pondicherry Railway Co. v. Commissioner of Income-tax, Union Cold Storage Co. Ltd. v. Adamson, Tata Hydro-Electric Agencies Ltd. v. Commissioner of Inland Revenue, Commissioner of Income-tax v. Tata Sons Ltd, Indian Radio & Cable Communications v. Commissioner of Income-tax and observed that those cases had no application to the facts which were then before the for their decision. On the other hand, their Lordships indicated that the cases of Commissioner of Income-tax v. Chandulal Keshavlal, Commissioner of Income-tax and Strong v. Woodfield should be applicable to the facts of that case. Their Lordships observed the ratio decidendi of the above cases was this :

These cases, therefore, show that if any amount is expended which is commercially expedient and is expended for the purpose of earning profits, it is a deductible expenditure."

In this case the commission payable is not linked with profits. Therefore, the rule laid down in Pondicherry Railway Co. Ltd. cannot and does not apply at all. Therefore, the only question is whether the rule laid down in Dharmvir v. Commissioner of Income-tax applies to the facts of this case. In this case the commission was paid in order to raise capital which the assessee-company needed badly. That it needed finance badly is evident by the fact that the turnover of the company increased immeasurably after the loan raised was utilised in the business. The loan was raised with a view to earn profits or more profits and save the assessee from losses. In other words, it was commercially expedient to pay the commission for raising the loan. Therefore, the commission paid was laid out or expended wholly and exclusively for the purpose of business.

Hence, in my view, if the question was wide enough to include the matter as to whether the expenditure was laid out or expended wholly and exclusively for the purpose of such business and the materials were properly before us, I would have held that the amount paid for commission was laid out or expended wholly and exclusively for the purpose of business.

In these views of the matter I respectfully dissent from the conclusions arrived at by my learned brother Mr. Justice Sinha, and am of opinion that the sum of Rs. 21,798 was not a capital

expenditure but a revenue expenditure deductible under section 10(2)(xv) of the Indian Income-tax Act.

BY THE COURT : Let this case be sent to the learned Chief Justice to constitute such Bench as he may consider fit.

BACHAWAT J - This case raises the question whether a certain payment by the assessee is of a capital or of a revenue nature. The assessee is a limited company. The assessee raised a loan of rupees ten lakhs by issuing debentures. By the debenture trust deed dated January 26, 1950, the assessee agreed that the loan would be redeemed in ten annual instalments of rupees one lakh each commencing from December 31, 1954. The debentures were issued at par and carried interest at the rate of 7 per cent per annum payable half-yearly. The loan was secured by mortgage of the movable and immovable properties of the assessee. The assessee had applied for and obtained the sanction of the Central Government to the proposed issue of debentures, as the issue of capital without such sanction was prohibited by section 3(2)(a) of the Capital Issues (Continuance of Control) Act, 1947, and as the issue and creation of the debentures and mortgage was an issue of capital within the meaning of section 2(b) read with section 2(e) of the Act. By another agreement of the same date the assessee agreed to pay to one Jogendra Lal Nundy and one Anil Krishna Pal, their respective heirs, executors, administrators, representatives and assigns, a commission at the rate of one percent. in perpetuity i.e. for ever on the gross sale of products of the mills of the assessee, such payment to be made immediately after the expiry of each year, the first payment to be made immediately after the 31 December, 1950. The assessee also agreed that the said Jogendra Lal Nundy and Anil Kumar Pal and their respective heirs etc., would be entitled to receive such commission even if the assessee company be reconstructed or taken over by anyone else. The preamble to the agreement recited that the assessee required a loan to the extent of ten lakhs for erecting its mills and purchasing plant, machinery, and stock-in-trade and for running the mill, that the assessee had approached the said Jogendra Lal Nundy and Anil Krishna Pal to secure the loan for the assessee on the express condition that if they could secure the loan the assessee would pay to them and their respective heirs, etc. a commission at the aforesaid rate in perpetuity, and that in consideration of their securing the loan the assessee executed the agreement. Jogendra Lal Nandy died on June 7, 1950, and was succeeded by his three sons. They, together with Anil Krishna Pal, and one Amar Krishna Poddar by deed dated the 10th December, 1951. During the accounting period relevant to the assessment year 1952-53, the assessee paid a sum of Rs. 21,798 as commission under the agreement aforesaid and claimed that the payment was an admissible deduction from the profits. The claim of the assessee was disallowed both by the Income-tax Officer and the Appellate Assistant Commissioner on the ground that the expenditure was of a capital nature. This finding was upheld by the Appellate Tribunal. The Tribunal found that the loan conferred on the assessee

a benefit of an enduring character and was, therefore, a capital asset in the hands of the assessee and that the amount of Rs. 21,798 paid by the aforesaid was an expense incurred in securing a loan capital and being in the nature of a capital expenditure was not an admissible deduction under section 10(2) (xv) of the Indian Income-tax Act, 1922. On the application of the assessee the Tribunal referred the following question of law to the High Court :

"Whether on the facts and in the circumstances of the case, the sum of Rs. 21,798 was a capital expenditure and, as such, not allowable as a deduction under section 10(2) (xv) of the Indian Income-tax Act."

The reference was heard by a Division Bench consisting of Sinha and Datta JJ. Sinha J. was of the opinion that the payment was in the nature of a capital expenditure and was not an allowable deduction under section 10(2) (xv) and that the question should be answered in the affirmative, whereas Datta J. was of the opinion that the payment was an allowable revenue expenditure. In view of this difference of opinion the matter has been placed before me èfor hearing.

Mr. Mitra appearing for the assessee contended that a loan is not a capital asset nor an advantage of an enduring character, that the loan is offset by the liability to repay it and that any expenditure incurred in connection with the raising of the loan must be held to be a revenue expenditure. Now in this case a loan of ten lakhs was raised by issuing debentures secured by a mortgage of the assessee's assets. The loan was required by the assessee for erecting its mills, purchasing its plant, machinery and stock-in-trade and for running the mill. The entire loan of ten lakhs was to endure for a fixed period of about five years and was thereafter repayable in ten annual instalments. The point in issue is whether the expenditure for raising a loan capital of this nature is of a capital or of a revenue nature.

Under section 10(2) (xv) of the Indian Income-tax Act, 1922, the expenditure is not an admissible deduction if it is "in the nature of a capital expenditure" In *In re Tata Iron and Steel Co. Ltd.* at page 1323, Shah J. very appropriately observed : in the nature of capital expenditure made the meaning of the expression more elastic in its application to the facts of each case."

The distinction between a capital and a revenue expenditure is not capable of precise formulation, At times the distinction is blurred and somewhat artificial. As between the payer and the recipient, it often matters very little whether the payment is of a capital or of a revenue nature. The matter becomes important when the revenue claims income-tax on the profits of the business carried on by the payer and the payer claims the payment as an admissible deduction. The point has to be determined from the ordinary business or accountancy point of view. If the expenditure is properly to be debited to the capital account, it would be of a capital nature, whereas if it is properly to be debited to the revenue account, it would be of a revenue nature. But

the question would then arise, what sum should be properly debited to the capital account rather than to the revenue account. In *British Insulated and Helsby Cables Ltd. v. Atherton Viscount Cave L.C.* formulated the following test :

"But there remains the question, which I have found more difficult, whether apart from the express prohibitions, the sum in question is (in the words used by Lord Sumner in *Ushers case*) a proper debit item to be charged against incoming of the trade when computing the profits of it; or in other words, whether it is in substance a revenue or a capital expenditure... But 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 a trade, I think that there is very good reason (in the absence of special circumstances leading to an opposite conclusion) for treating such an expenditure as properly attributable not to revenue but to capital."

In that case Viscount Cave held that a lump sum amount paid by the assessee out of current profits to the trustees of a pension fund with a view to create the nucleus of pension fund for the benefit of the assessee's employees was in the nature of capital expenditure, and was not an admissible deduction, even though the amount was expended wholly and exclusively for the purpose of the trade and even though the deduction of the amount from the profits was not expressly prohibited by the English Income-tax Act, 1842. Our Supreme Court has approved of the test laid down by Viscount Cave. In *Assam Bengal Cement Co. Ltd. v. Commissioner of Income-tax* Bhagwati J. observed :

If the expenditure is made for acquiring or bringing into existence an asset or advantage for the enduring benefit of the business it is properly attributable to capital and is of the nature of capital expenditure. If on the other hand it is made not for the purpose bringing into existence any such asset or advantages but for running the business or working it with a view to produce the profits it is a revenue expenditure... The expression "once and for all" is used to denote an expenditure which is made once and for all for procuring an enduring benefit to the business as distinguished from a recurring expenditure in the nature of operational expenses."

Applying the test formulated above, I should hold that the loan of Rs. 10,00,000 was an asset or advantage for the enduring benefit of the business of the assessee. The loan was raised by the issue of mortgage debentures and was to endure for a fairly long period and was not a borrowing of money on a temporary or short term basis such as is necessary and incidental to the ordinary course of the assessee's business. The loan was required by the assessee for erecting its mills, purchasing its plant, machinery and stock-in-trade and for running the mill. Like all loans, the loan had to be repaid after the stipulated period expired, but during the period the loan endured, the assessee secured a powerful instrument of earning profits. During the period of the loan, the capital structure of the assessee was expended and the assessee had better means of earning

profits of a more or less permanent character. The raising of the loan was a financial operation unconnected with the day-to-day business activities of the assessee. The expenses incurred in connection with the raising of the loan cannot be regarded as operational expenses or as trading expenses or as expenses incidental to the business. The commission payable for negotiating and securing the loan is prima facie and, in the absence of cogent and compelling reasons leading to an opposite conclusion, an expense of a capital nature.

The decided cases appear to support the conclusion that the expenses incurred in connection with the raising of such a loan are in the nature of a capital expenditure. In *Nagpur Electric Light and Power Co. Ltd. v. Commissioner of Income-tax* it was held that the stamp, registration and legal expenses and the brokerage paid for negotiating a debenture loan of Rs. 6,00,000 required by an electric light and power company were "expenses" of a capital nature and the purposes for which the loan was required were treated as immaterial. In *Western India Plywood Ltd. v. Commissioner of Income-tax* the Kerala High Court held that the amount of underwriting commission, stamp, registration, and legal expenses paid in connection with the raising of a working capital of Rs. 3,00,000 by the issue of first mortgage debentures redeemable in three successive equal annual instalments was an expense of a capital nature and that the character of the expenditure was not to be judged by the subsequent use of the loan. In *Vizagapatnam Sugars and Refinery Ltd. v. Commissioner of Income-tax*, the Andhra Pradesh High Court held that the payment of a recurring commission to persons negotiating a mortgage debenture loan of Rs. 2,50,000 was an expense of raising a loan capital and was not an allowable deduction. In *Commissioner of Income-tax v. India Cements Ltd.* the Madras High Court held that the stamp registration and legal and other charges incurred for raising a mortgage loan of Rs. 40,00,000 repayable in ten annual instalments was not a revenue expenditure, stress being laid on the fact that out of the loan, a sum of Rs. 25,00,000 was required for discharging a previous loan which had been utilised for capital assets, and as to the balance of Rs. 15,00,000 there was no material on the record to show how it was spent.

The English cases on the subject mostly turn on the construction of an express statutory prohibition declaring that no sum shall be deducted in respect of or on account of "any capital withdrawn therefrom no for any sum employed or intended to be employed as capital in such trade, manufacture, adventure or concern" or similar words of prohibition in the successive English Income Tax Acts and particularly, in the Income Tax Act, 1842(5&6 Geo. Vict. c. 35), section 100, Schedule D, Case 1, rule 3, the Income Tax Act, 1918 (8 & 9 Geo. Vict. C. 40), Schedule D, Rules applicable to Cases I and II, r. 3(f), and the Income Tax Act, 1952 (15 & 16 Geo. 6 & 1 Eliz. 2, c. 10), section 137(f). In view of such an express statutory prohibition, it has been held that no sum could be deducted on account of payment of (a) the interest on partners borrowed capital : see *Anglo-Continental Guano Works v. Bell*, (b) the commission and fees paid

to agents and brokers and the expenses of stamps postage, printing advertising and law charges incurred in arising a loan capita by the issue of debenture and debenture stock by a mortgage company : see *Texas Land and Mortgage Company v Holtham*, (c) the interest on working capital borrowed by a financing company to meet the growing demands of its business : see *European Investment Trust Co. Ltd. v. Jackson*, (d) commission paid in respect of a financial guarantee for a loan secured by the issue of a first mortgage debenture stock : see *Ascot Gas Water Heaters Ltd. v. Duff*, (e) premium on repayment of a loan secured by a legal charge and obtained by a firm of estate developers to acquire and develop an estate : see *E. J. Bridgwater and W. H. Bridgwater v. King*. The ratio of these decisions is that those payments were in respect of sums employed or intended to be employed as capital in the trade. Since the decision in *Farmer v. Scottish North American Trust Ltd.*, a distinction has been drawn between loans which, although capital, were temporary in their nature and might be regarded as an ordinary incident of carrying on the business of the borrower and other loans, and deduction have been allowed for sums spent in respect of loans of the former kind, e.g., (a) interest on a short-term and fluctuating overdraft taken from bankers by an investment company, the daily borrowing the lending of many being part of the borrowers business : see *Farmers case*, and (b) commission paid for a guarantee in respect of an existing trade debt of the assessee company to be repaid as quickly as possible : see *Ascot Gas Water Heaters Ltd. v. Duff*. The decisions of the English courts in so far as they are based upon the aforesaid express statutory prohibition cannot be applied in this country in the absence of a similar statutory prohibition. Furthermore, section 10(2) (iii) of the Indian Income-tax Act, 1922, expressly permits deduction of the interest paid in respect of capital borrowed for the purposes of the business and it makes no difference that the interest paid is in respect of debentures issued in lieu of the purchase price of shares : see *Eastern Investments Ltd. v. Commissioner of Income-tax*. Several other decision cited at the Bar proceed upon somewhat different grounds. Thus in *Montreal Coke and Manufacturing Co. v. Minister of National Revenue* it was held that the expenses of the issue of new bonds at lower interest rates and on less onerous conditions upon redemption of the existing bounds including the payments on account of the premium on redemption, exchange, discount to underwriters, overlapping of interest, legal, printing and other charges were not disbursements for the purpose of earning the income within the meaning of section 6(a) of the Canadian income War Tax Act, 1927, since it was not the business of the assessee to engage in financial operations and their deduction was prohibited by section 6(a), but Lord Macmillan preferred not to decide whether the expenses were a payment on account of capital and therefore struck by section 6(b) also. In India the bonus paid to the debentureholders in similar circumstances has been held to be a capital expenditure : see *Associated Hotels of India Ltd. v. Commissioner of Income-tax*. In *London County Freehold and Leasehold Properties v. Sweet* it was held that the expenses incurred by an investment company in the issue of new debenture stock for the purpose of repaying the existing debentures,

specific mortgages, bank loans and other charges, were expenses of rearrangement of the loan capital, and like the expenses of raising loan capital could not be regarded as expenses of management within the meaning of the section 33(1) of the Income Tax Act, 1918. In *Small v. Easson* the expenses of the transfer of a mortgage of the business premises owned by the assessee was held not to be deductible under the English Income Tax Act, 1842, and it is notable that Lord Justice Clerk (Scott Dickson) rested his individual judgment on the ground that the payment was in the nature of capital expenditure in the sense in which that term was used by Lord Dunedin in the *Vallambrosa Case*. A similar question in our country must be resolved with reference to section 10(2) (xv) of the Indian Income-tax Act, 1922. In *Bhadani Brothers Ltd. v. Commissioner of Income-tax* the expense of perfection a pledge to secure a loan raised for the acquisition of managing agency rights was regarded as part of the expenses of acquisition of the capital asset and not an admissible deduction.

In the case of *In re Tata Iron & Steel Co. Ltd.* it was held that a payment of commission for underwriting the issue of new shares was part of the raising new capital and was in the nature of a capital expenditure and not an allowable deduction under section 10(2)(xv). The subsequent decisions in this country proceed on the footing that there is no substantial distinction between the raising of the share capital and the raising of a loan capital of a more or less permanent nature by the issue of debentures or upon the security of a mortgage. The case of *Dharamvir Dhir v. Commissioner of Income-tax*, relied upon by Mr. Mitra, is distinguishable. In that case the assessee had secured a loan for his business upon the term that he would pay to the lender a sum equivalent to 11/16th of the net profits of his business, in addition to interest at six per cent per annum, and it was held that the amount paid on account of the 11/16th share of the profits was an expenditure incurred for the carrying on the assessee's business and was therefore wholly and exclusively laid out for the purposes of his business and was an allowable revenue expenditure. It will be noticed that the 11/16th share of the profits was payable for the use of the loan capital and was not a cost of acquisition of the capital. By the express words of section 10(2)(iii) interest for the use of loan capital is an allowable deduction, and on general principles, any further sums payable on account of the use of the capital would also be an allowable deduction. The principle is that a price paid, whether in lump sum or in instalments for the acquisition or purchase of a capital asset of a business, is a capital expenditure, but a fee or rent or other monies paid for the use of the capital asset is a revenue payment.

Prima facie, the expenses of raising the loan capital in the instant case are of a capital nature. Nevertheless, Mr. Mitra argued that the amount of the commission payable for procuring the loan is of a revenue and not of a capital nature because the payment (1) is perpetual, (2) will continue after the loan is repaid (3) is related to the turnover of the assessee's business, and (4) is not related to any agreed capital sum. I am unable to accept this contention.

In support of his argument Mr. Mitra relied upon the case of Commissioner of Inland Revenue v. 36/49 Holdings Ltd., where in consideration of the sale of all the shares in R. L. Ltd., the assessee became entitled to be paid by the buyers various sums including the sums of Rs. without deduction for each mechanically propelled bicycle and pound 1 without deduction for each motor bicycle sold by R. Ltd, or the buyers or one E.M.I. Ltd. or their subsidiary companies under clause 2(A) (vii) of the agreement, with an option to the buyers to commute those payments on payment of named sum in cash within a certain period and on condition that unless so commuted the payments would continue at all times thereafter. Macnaghten J. held that the payments under clause 2(A) (vii) resembled an annuity and were income in the hands of the assessee; and his decision was affirmed by the Court of Appeal, Lord Greene M. R. observing that (a) unless the right to commute was exercised, the payment would be going on in perpetuity and that it was difficult to class under the category of "capital" a perpetual payment, (b) that the payments being related to turnover, i.e. to a trading activity of R. Ltd., was not dissimilar from royalties on patents, (c) that the sums payable were not related in any way to any special sum, and that (d) the payment which might continue in perpetuity could not be regarded as a payment by instalments of a capital sum. This case was concerned with the question whether a certain receipt was capital or income in the hands of the recipient and not within the question whether a payment was in the nature of capital or revenue expenditure.

Mr. Mitra, however, strongly relied upon the decision of the Bombay High Court in Commissioner of Income-tax v. Kolhia Hirdagarh Co. Ltd. The facts of that case were somewhat complicated, but to put the matter briefly the assessee had required the business of the colliery as a going concern together with its goodwill, mining lease and licences. The purchase price was fixed at rupees one lakh which was to be discharged by the payment of a sum of Rs. 75,000 in cash and the allotment of fully paid shares of the face value of Rs. 25,000 to the vendor. The Tribunal found that the agreed price of rupees one lakh did not include the valuation of the goodwill and the mining lease and licences. The assessee ultimately also agreed to pay to the vendor commission at the rate of four annas per ton of steam and rubble coal and three annas per ton of sleek coal raised from the colliery and sold and relied by the assessee from the colliery. The Tribunal found that the commission was payable to the vendor in consideration of the latter making available to the assessee the user of the mining lease and licences and held that the amount of commission paid by the assessee was a revenue and not a capital expenditure. The Bombay High Court agreed with this conclusion. Chagla C.J. thought that he should follow the decision in Commissioner of Inland Revenue v. 36/49 Holdings Ltd. and observed : "... I think on the whole I would take the same view as the court of Appeal took in that case and hold that as the payment made by the assessee is a payment made for an indefinite period, a payment made in relation to the turnover of the company and not in relation to its profits, and as this payment has no bearing to any specific sum fixed as part of the price for the purchase of the undertaking, this

payment is in the nature of revenue payment and not capital payment."

Now it is to be noticed that in the Bombay case the Tribunal had found that the expenditure in question was of *à* revenue nature and the Bombay High Court refused to interfere with that finding; whereas in the instant case the Tribunal has found that the disputed payment is in the nature of a capital expenditure and I am asked to disturb that finding. The next thing to be noticed is that Chagla C.J. distinguished various cases cited before him on the ground that those cases were concerned with the question whether certain receipts were capital or income in the hands of the recipient and not with the question whether a payment was in the nature of capital or revenue expenditure, but curiously he found that in all its important and significant aspects the case before him was indistinguishable from the case of Commissioner of Inland Revenue v. 36/49 Holdings Ltd. and based his own conclusion entirely upon that decision, quite overlooking that the aforesaid decision was also concerning the nature of a receipt in the hands of a recipient and not concerning the nature of a payment in relation to the person making the payment. This point was brought out forcibly by Chakravarti C.J. in National Cement Mine Industries Ltd. v. Commissioner of Income-tax. Thirdly, I think that the principles which determine the nature of a receipt in the hands of the recipient are not relevant in determining the character of the payment in relation to the person making the payment. The case of Commissioners of Inland Revenue v. 36/49 Holdings Ltd. guides us in determining whether a periodic receipt is capital or income in the hands of the recipient. If a seller agrees to accept a series of payments in lieu of the price, the recurring receipt is income in his hands, if it is truly the produce or return of an investment of capital. The case of Commissioners of Inland Revenue v. 36/49 Holdings Ltd. shows that if the receipts is perpetual, is related to the turnover of a trade and is not related to any agreed capital sum, the case for holding that the receipt is income is to that extent stronger. So also is the case of National Cement Mines Industries Ltd. Commissioner of Income-tax affirming [1956] 29 I.T.R. 629, where the receipt of a recurring payment of thirteen annas per ton of cement sold by the buyer was found to be income in the hands of the seller. But each case must be decided on its own individual facts and the recurring receipts may be truly an instalment of capital in the hands of the seller, though the payment is perpetual or is during the life of the seller or is related to the turnover to the profits of a business e.g. a perpetual payment of ten per cent. of the oil produced from the land sold; see Minister of National Revenue v. Spooner or ten annual payments of 25 per cent. of the profits of the dental practice sold : see Inland Revenue Commissioners v. Ramsay of 250 during the life out of the creditor in settlement of the money owed : see Dott v. Brown. But quite different considerations arise when we have to determine whether the payment should be regarded as a revenue or a capital expenditure in relation to the person making payment. In Associated *è*Portland Cement Manufacturers Ltd. v. Inland Revenue Commissioner, Lord Greene M.R. observed :

"Whether or not an item of expenditure is to be regarded as of a revenue or capital nature must in many, and, indeed, in the majority of cases, I should have thought, depend upon the nature of the asset or the right acquired by means of that expenditure."

In Assam Bengal Cement Co. Ltd. v. Commissioner of Income-tax Bhagwati J. observed :

"If any such asset or advantage for the enduring benefit of the business is thus acquired or brought into existence it would be immaterial whether the source of the payment was the capital or the income of the concern or whether the payment was made once and for all or was made periodically. The aim and object of the expenditure would determine the character of the expenditure whether it is a capital expenditure or a revenue expenditure. The source or the manner of the payment would then be of no consequence."

Even a recurring expenditure would be of a capital nature, if the aim and object of the assessee is to acquire a capital asset for the enduring benefit of the trade. The character of the expenditure is not changed because (a) the payment will continue after the capital asset so acquired is exhausted or because (b) the amount is dependent on the trading activities of the assessee and is neither ascertained nor ascertainable or because (c) the amount is payable out of a portion of receipts of the assessee's business irrespective of his earning profits from the business as a whole or because (d) the payment is made not to the vendor of the capital asset but to a third party. Thus in *Bean v. Doncaster Amalgamated Collieries Ltd.* the payment of the expense of a general drainage improvement scheme in sixty half-yearly instalments was regarded as capital expenditure, though the coal measures benefited by the scheme worked out in some six or seven years : see the judgment of Uthwatt J. at page 309. In *Vizagapatnam Sugars & Refinery Ltd. v. Commissioner of Income-tax* the payment of a recurring commission of four annas per Bengal maund of sugar sold by the assessee for twenty years was found to be an expense of a capital nature. In *Delage v. Nuggett Polish Company Limited*, by virtue of an agreement the defendants had the exclusive right of selling and manufacturing articles by a secret process and were to pay to the plaintiffs for forty years 8 per cent. on the gross receipts of such sale. The plaintiffs resided abroad and were foreigners and before paying the amount payable to them under the agreement the defendants deducted income-tax in respect of the amount and it was held that the receipt was income in the hands of the plaintiffs and also the income-tax was rightly deducted. One of the points in issue was whether the defendants had been rightly compelled by the Crown to pay income-tax on their profits without deducting the payments made by them under the agreement. It was held that the defendants were rightly so completed as the payments were capital expenditure. The fact that the payments were fluctuating sums related to the trading activities of the taxpayers did not change their essential character. Phillimore J. observed :

"They were compelled by the Crown, and as it seems to rightly compelled by the Crown, to pay

on their net profits without deducting the sum of money which they had to pay away as the 8 per cent. Rightly were they so compelled because that sum of money was at any rate as between the Crown and the tax payer to be viewed as no deduction from profits, but as part payment in the way of capital expenditure for the article originally bought, out of which they made their profits. Having been so compelled, and having therefore paid upon the net profits without deduction, they seek when they came to pay the 8 per cent. over to the plaintiffs to take from that 8 per cent. income tax at the rate in force in 1903."

The case also illustrates the point that the same payment may be a capital expense in relation to the payer and an income receipt in the hands of the recipient. In *Tata Hydro-Electric Agencies Limited. v. Commissioner of Income-tax on appeal from [1936] 4 I.T.R. 92*, the facts were that the appellants had acquired their agency business by assignment from their predecessors, Tata Sons Ltd. subject to certain agreements by which their predecessors who had procured loans for the managed company Messrs. Tata Power Co. Ltd. had agreed to pay of each of the two lenders, in addition to the interest payable on the loans by the Tata Power Co. Ltd. 12 1/2 per cent of the commission of 10 percent on the annual net profits of the Tata Power Co. Ltd. receivable by Tata Sons Ltd. under their agency agreement for 41 years. Subsequently the appellants entered into direct agreements with the Tata Power Co. Ltd. and with the lenders on terms identical with those of their agreements with Tata Sons Ltd. The Privy Council held that the amount of the 25 per cent. commission payable to the two lenders was not an expenditure incurred solely for the purpose of earning the profits of the appellants business and was not an admissible deduction as those payments had been undertaken by the appellants in consideration of the purchase of the managing agency rights. It did not matter that the undertaking was to pay not to the vendor but to a third out of a particular receipt of the appellants business irrespective of their earning any profits from the business as a whole.

On principle I see no reason why a perpetual payment of fluctuating annual sums dependent on the turnover of the assessee's business cannot be an expense of a capital nature. The assessee may have submitted to a hard bargain, but if he undertakes to make the recurring payment with a view to acquire a capital asset, the payment is a capital expenditure. In my opinion the commission payable under the agreement dated the 26th January 1950, for services rendered for procuring the loan capital is in the nature of a capital expenditure, though the payment (1) is perpetual in the sense that it will continue so long as the products of the assessee's mills are sold, (2) may thus continue ever after the loan is repaid, (3) is related to the turnover of the assessee's business, and (4) may not be related to any named sum. The payment of the commission is not an item of the cost of manufacture or of trading and is no part of the operational expenses of the assessee's business. There is no evidence on the record to show that such an item is properly debitable to the revenue account either from the business or from the accountancy point of view.

The Tribunal held that the payment was in the nature of a capital expenditure and it is not shown that on the facts found by the Tribunal its final conclusion is erroneous in law.

I am, therefore, of the opinion that, on the facts and in the circumstances of the case, the amount of Rs. 21,798 was a capital expenditure, and as such not an allowable deduction under section 10(2)(xv) and that the question asked should be answered in the affirmative. I agree with the opinion and conclusions of Sinha J. and I would respectfully record my dissent from the opinion and conclusion of Datta J. It is now my duty to return my opinion so that the referring Bench Pronounce the final decision in the case.

I pass the following under :

Let the matter together with my opinion be now placed before the Chief Justice for necessary action so that final orders may be passed by the appropriate Division Bench.

Question answered in the affirmative.