

(1978) 07 AHC CK 0031

In the Allahabad High Court

Case No : Income-tax Reference No. 130 of 1974

Ram Kumar Pharmaceutical Works

APPELLANT

Vs

Commissioner of Income Tax

RESPONDENT

Date of Decision : 12-07-1978

Acts Referred:

Income Tax Act, 1922 — Section 10(2)

Citation : (1979) 8 CTR 168 : (1979) 119 ITR 33

Hon'ble Judges : Satish Chandra, C.J.;K.C. Agrawal, J

Bench : Division Bench

Advocate : V.B. Upadhy, for the Appellant; A. Gupta, for the Respondent

Judgement

Satish Chandra, C.J.—The assessee, M/s. Kumar Pharmaceutical Works, is a registered firm carrying on business, inter alia, in the manufacture and sale of saccharine. On February 6, 1961, it entered into an agreement with Heyden, a West German concern. Under this agreement, Heyden was to transmit to the assessee know-how and data for construction and operation of a plant for the manufacture of saccharine by flow-sheet process. For cession of the know-how and data, Kumar was to pay to Heyden a sum of DM 10,000 immediately on the conclusion of the agreement and, in addition, for the next five years, a royalty of 2 1/2% on the sale value of the manufactured products, subject to the maximum of DM 35,000.

2. For the assessment year 1966-67, the assessee paid Rs. 28,917 as royalty to Heyden. It claimed deduction on the ground that it was a revenue expenditure. This was disallowed, and the disallowance was affirmed in appeal as well as by the Tribunal on further appeal. The Tribunal held that the payment was of a capital nature. Under the agreement, the assessee obtained the right to use the know-how and the data for ever in future. The assessee paid to Heyden the costs of the know-how and the data. The royalty was in reality an instalment payment of the purchase price of the technical know-how. The payment was a part payment for the acquisition of the technical knowledge. It was of a capital nature.

3. At the instance of the assessee, the Tribunal has referred for our opinion the following question:

"Whether, on the facts and in the circumstances of the case, the sum of Rs. 28,917 constituted an item of revenue expenditure or capital expenditure ? "

4. The terms of the agreement are quite clear. Heyden parted with the know-how and the data for setting up and operating a plant for production of saccharine by the flow-sheet process. This know-how and the data was transferred to the assessee for being used by it in future without any limit of time. The only restriction placed upon the assessee's right to use it was that it could not transfer it to anyone else, and that it had to keep it secret. For the transfer of "cession" of this know-how and the data, the assessee paid cash consideration. A part of it was paid immediately, the rest was to be paid over a period of five years. It is evident that the assessee acquired ownership of the know-how and the data. It was not merely entitled to use it only so long as it continued to pay the royalty. This was a case of acquisition and not merely user for a limited time. The assessee clearly obtained an advantage of an enduring nature. The payment for its acquisition was clearly capital in nature.

5. Learned counsel for the assessee relied upon BOMBAY STEAM NAVIGATION CO. (1953) PRIVATE LTD. Vs. COMMISSIONER OF Income Tax, BOMBAY., , where the question was as to what was the significance of the expression " capital" in the context of " capital borrowed " in Section 10(2)(iii) of the Indian I.T. Act, 1922. No such problem arises before us. In that case, the Supreme Court observed that no uniform formula or test can be laid down for ascertaining whether an expenditure is capital or revenue because the determination of such a question would depend upon the facts and circumstances of each case. The court has to consider the nature and ordinary course of business and the objects for which the expenditure is incurred.

6. Applying this test, it is apparent that the object for which the expenditure was incurred was to obtain a right of an enduring nature. The object was to acquire a capital asset. The expenditure was in nature capital.

7. The decision in Commissioner of Income Tax, Bombay Vs. Ciba of India Ltd., is equally distinguishable. There, one of the terms of the agreement was that upon termination of the agreement for any cause, the Ciba company would cease to use the patents and trade marks and return to the Swiss company all copies of information, scientific data or material sent to it. The agreement was for a period of five years for which an annual royalty was to be paid. Here the royalty was to be paid for use for a temporary period for know-how and data. The assessee in that case did not acquire ownership of such know-how or data.

8. The case of Commissioner of Income Tax Vs. Lucas-T.V.S. Limited (No. 1), is equally unhelpful. Here also the term of the agreement of technical collaboration was that after the expiry of the period of licence, the stock remaining in hand was to be sold and royalty way payable therefor. It was found that the assessee

had no right to manufacture fresh articles on the basis of know-how which it had obtained from the foreign company, after the termination of the agreement. The payments were held to be in the nature of a licence fee for the period the agreement remained in force. For the reasons already mentioned, this case is also equally distinguishable.

9. We answer the question referred to us by holding that a sum of Rs. 28,917 did, in the circumstances of the case, constitute an item of capital expenditure. The Commissioner will be entitled to costs which are assessed at Rs. 200.