A

DEVIDAS VITHALDAS & CO.

v.

C.I.T., BOMBAY CITY

January 28, 1972

B

[S. M. SIKRI, C.J., J. M. SHELAT, H. R. KHANNA AND G. K. MITTER, JJ.]

Income-tax—Capital or Revenue expenditure—Goodwill—Deed of dissolution of partnership reciting "sale" of goodwill in consideration of share in the profits—Payment not related to any lump-sum fixed as purchase price—Duration of payment indefinite and amount indefinite—
C *Payment made by vendee if admissible deduction as revenue expenditure.*

P and A carried on business as Chartered accountants in the name of D.V. & Co. On P retiring from partnership a deed of dissolution was executed which provided that the business would be carried on by A. By clause 2 of the deed, P, who owned the rights and interest in the goodwill, "agreed to sell" the goodwill to A and "as consideration
D for and in full satisfaction of the purchase price of the goodwill" A was to pay eight annas in the rupee in the net profits of the business payable during the life time of P and after him during the life time of his wife and then to their son during his life time. Clause 6 provided that in the event of A entering into partnership or transferring or assigning his business so long as the business was carried on in the name of D.V. & Co., the partnership, the assignee or the transferee was to pay the share in the profits in the manner provided in cl. (2). A entered into partnership
E with C, the deed of partnership reciting that the goodwill of the business belonged solely to P which A had "bought" in consideration of his agreeing to pay a share of eight annas in the rupee and that the parties thereto pay five annas four pies share in the profits, by way of purchase price of the goodwill as agreed by P. The firm paid to P's wife, after the death of P, various amounts during the years 1955-59. It claimed that those amounts should be deducted in its assessments for those years. The Income-tax Officer and the Appellate Assistant Commissioner re-
F jected the claim holding that the payments were capital and not revenue payments and the transaction evidenced by the deed of dissolution was one of outright sale. On appeal, the Tribunal held that the payments constituted only fee or rent for the use of the goodwill so long as it was used and accordingly they were in the nature of revenue expenditure. On reference the High Court answered in favour of the Revenue.

G

Allowing the appeal,

HELD : (Sikri C.J. Dissenting) On the facts of the case the transaction was a licence and not a sale of the goodwill; the disbursements in question, therefore, were in the nature of royalty and must be treated as admissible deduction. [232 B]

(i) There is no single test of universal application for deciding the question whether an agreement is for payment of price in stipulated
H instalments or for making annual payment in the nature of income and, therefore, the Court has to look not only into the document relating to the transaction, but also the surrounding circumstances to decide its true nature, the name which the parties give to it being of little consequence.

This does not mean that the legal character of the transaction which is the source of the receipt in question can be ignored and substituted by what the taxing authority considers the substance of the matter. [224 B] A

Travancore Sugars and Chemicals Ltd. vs. *C.I.T.*, (1966) 62 I.T.R. 566, referred to.

(ii) One of the tests Courts have applied in distinguishing between capital and revenue expenditure is whether the expenditure in question was for bringing into existence an asset or an advantage of "an enduring nature", and is made "once and for all". It may be payable not necessarily all at once but even by instalments as against a recurrent expenditure in the nature of operational expenses. The question in such cases would be, is the expenditure the assessee's working expenditure laid out as part of the process of profit earning or a capital outlay necessary for the acquisition of a property or rights of a permanent character the possession of which is a condition of carrying on the trade. But the expressions "enduring benefit", and rights of a permanent character are only descriptive and not definitive and are relative in meaning, not synonymous with 'perpetual' or 'everlasting'. The expression "enduring benefit" is thus a relative term not enduring in the sense of its being permanent, but is sufficiently durable depending upon the nature of the terms upon which it can be acquired. So also the the expression "once and for all" which does not mean payment at one time of the whole amount but includes payment of a lump-sum, as distinct from recurrent, distributed in periodic instalments. [22 F] B C D

Atherton v. *British Insulated and Helsby Cables Ltd.*, 10 T.C. 155; *Assam Bengal Cement Co. Ltd.* v. CI..T. 27 I.T.R. 34, 46; *Robert Addie and Sons' Collieries Ltd.* v. *Commissioner of Inland Revenue*, 8 T.C. 671; *Commissioner of Taxes* v. *Nchanga Consolidated Copper Mines Ltd.*, (1965) 58 I.T.R. 241; *C.I.T. West Bengal* v. *Coal Shipment (P) Ltd.*, *Civil Appeals Nos.* 1494 to 1498 of 1971, decided on October 14, 1971; *C.I.T.* v. *Finlay Mills*, (1951) 20 I.T.R. 475; *Henriksen* v. *Grafton Hotel Ltd.*, 24 T.C. 453 and *Strick* v. *Regent Oil Co. Ltd.*, 43 T.C. 1, 38 referred to. E

The other test sometimes applied, is payment when it is referrable to fixed capital or capital assets as against payment referrable to circulating capital or stock-in-trade. This test also is not capable of being treated as of uniform application. [226 F] F

Assam Bengal Cement Co. Ltd. v. C.I.T., 27 I.T.R., 34, 46, referred to.

(iii) Acquisition of the goodwill of a business is, without doubt acquisition of a capital asset, and therefore, its purchase price would be capital expenditure. It would not make any difference whether it is paid in a lump-sum at one time or in instalments distributed over a specific period. Where, however, the transaction is not one for acquisition of the goodwill but, for the right to use it. the expenditure would be a revenue expenditure. [226 H] G

In Re Ramjidas Jaini & Co., (1945) I.T.R. 430; *Kuppuswami* v. *C.I.T.* (1954) 25 I.T.R. 349; *Ogden* v. *Medway Cinemas Ltd.*, 18 T.C. 691; *The Secretary of State for India* v. *Scoble*, [1903], A.C. 299; *Jones* v. *Commissioner of Inland Revenue*, 7 T.C. 310; *Commissioner of Inland Revenue* v. *Ramsay*, 20 T.C. 79; *Vithaldas Thakerdas and Co.* v. C.I.T., [1946] I.T.R. 822 and *Travancore Sugars and Chemicals Ltd.* v. *C.I.T.*, (1966) 62 I.T.R. 566, referred to. H

A (iv) In the present case even though Cl. (2) of the deed of dissolution uses expressions such as "agreed to sell" and "the purchase price of the goodwill," these expressions are not determinative of the exact nature of the transaction or the relationship between the parties arising therefrom. Clause (2), no doubt, prescribes the mode and the quantum of payment. But, the duration of payment is indefinite and secondly the amount is indefinite depending upon the rise and fall in the profits of the business. The B payment is not related to any lumpsum fixed as the purchase price. But on the contrary it is directly related to and dependent upon whether at all and what profits are made. Further, the document is totally silent as to what is to happen to the goodwill if A, or his partners, if he were to enter into a partnership, cease to carry on the business in the name of D.V. & Co. The transaction thus contains all the grounds given in the case of *Travancore Sugars and Chemicals Ltd.*, upon which this Court concluded that such payments could not be treated as capital disbursement, namely, C an indefinite period, absence of any expressed lumpsum and payment relating to profits and not being tied up with any fixed sum agreed to as the purchase price of the capital assets. [230 F-H; 232 B]

Travancore Sugars and Chemicals Ltd. v. *C.I.T.* (1966) 62 I.T.R. 566 applied.

(v) Quite apart, Cl (6) itself contains indication of the transaction D not being an outright purchase of the goodwill. If the transaction was an outright purchase of goodwill there was no necessity of Cl. (6) providing for the partnership which A would enter into or his assignee or transferee having to pay the share so long as he or they continued to carry on business in that name. [231 B]

Per Sikri, C.J. dissenting.

E (i) Clause (2) of the dissolution deed says what it meant to convey, that is, there is an agreement to sell and sale of the goodwill of the partnership. The words "as consideration for and in full satisfaction of the purchase price of the goodwill" cannot be watered down by any of the subsequent clauses. Further, the deed executed by A and C also recited that A had "bought" the goodwill in consideration of his agreeing to pay a share of the profits. It is difficult to go against the express F wording of the deed when there is no clear clause overriding these words. [216 E]

(ii) A mode of payment of purchase price of any capital asset cannot convert a capital payment into a revenue payment in the hands of the vendee. It may be that the mode of payment may affect the character of the receipt in the hands of the vendor. [218 H]

G (iii) The grounds adopted by this Court in *Travancore Sugars and Chemicals Ltd.* cannot be regarded as conclusive in a case where there can be no doubt that the capital asset has been sold. [219 B-C]

The absence of a clause providing what is to happen if the vendee of the goodwill ceases to carry on the business further reinforces the conclusion that it was an out and out sale. This clause was not inserted because it would be out of place in a case of sale. [219 D]

H (v) Clause (6) does not have any bearing on the question under consideration. This clause has been inserted in order to safeguard the interest of the vendor who was keen to see that he would get as much as possible for the sale of the goodwill. [219 F]

Therefore, on the facts, the goodwill was an asset of an enduring nature. The fact that payment was to be made over a number of years and the nature of a chartered accountant's business lead to this conclusion. [219 F] A

CIVIL APPELLATE JURISDICTION : Civil Appeals Nos. 1452 to 1455 of 1968.

B

Appeals from the judgment and order dated February 25, 1967 of the Bombay High Court in Income Tax Reference No. 49 of 1962.

M. C. Chagla, Bhuvanesh Kumari, J. B. Dadachanji, O. C. Mathur and Ravinder Narain, for the appellant (in all the appeals).

C

N. D. Karkhanis, R. N. Sachthey and *B. D. Sharma,* for the respondent (in all the appeals).

SIKRI C.J. delivered a dissenting opinion. The Judgment of SHELAT, KHANNA and MITTER, JJ. was delivered by SHELAT, *J.*

Sikri, C.J., I have read the draft of the judgment prepared D by Shelat J., but I regret I am unable to agree with his conclusions. He has set out all the relevant facts and the relevant documents and it is not necessary for me to burden my judgment with them.

It seems to me that there is no difficulty in interpreting clause 2 of the dissolution deed. It says what it meant to convey, that is, E there is an agreement to sell and sale of the goodwill of the partnership which belonged to Padamsi alone to Amratlal. It is difficult to water down the words "As consideration for and in full satisfaction of the purchase price of the goodwill" by any of the subsequent clauses.

Reliance is placed on the deed dated October 18, 1955, F executed by Amratlal and one Chandrakant V. Parikh. This deed also recited that "the goodwill of the said business belonged solely to the said Padamsi which he, the said Amratlal, had 'bought' in consideration of his agreeing to pay a share of eight annas in the rupee to Padamsi". I find it again difficult to go against the express wording of the deed when there is no clear G clause overriding those words. I am not averse to discovering the substance of a transaction but there is a limit to the extent I can disregard the language in a commercial document. Reliance is placed on clause 5 of this deed. I am unable to say that this clause has the effect of converting a sale into a licence. It is argued that the mode of payment of the purchase price shows that it was not a purchase. I am unable to see how a mode of H payment of purchase price of any capital asset can convert a capital payment into a revenue payment in the hands of the vendee.

A It may be that the mode of payment may affect the character of the receipt in the hands of the vendor but as far as the vendee is concerned, I am unable to agree that the mode of payment can convert what is obviously a capital payment or expenditure into a revenue payment or expenditure. Reliance was placed on the three grounds adopted by this Court in *Travancore Sugars &* B *Chemicals Ltd.* v. *C.I.T.*(1) *viz.*, indefinite period, absence of any expressed lump sum, and payment relating to profits and not being tied up with any fixed sum agreed to as the purchase price of a capital asset. I am unable to regard these grounds as conclusive in a case where there can be no doubt that the capital asset has been sold. If A sells his house to a company for its C office and stipulates that in full satisfaction of the purchase price he will receive annual payments relating to profits without stipulating for a fixed sum, I doubt if anybody will argue that the company can deduct the annual payments as revenue expenditure. The fact that it is a sale of a capital asset like goodwill does not make any difference.

D It was urged that it is not really an out and out sale of goodwill because there is no clause providing what is to happen if the vendee of the goodwill ceases to carry on the business. To my mind, the absence of such a clause further reinforces the conclusion that it was an out and out sale. This clause was not inserted because it would be out of place in a case of sale.

E Reliance was also placed on clause 6 which has been set out in detail in the judgment of Shelat J. In my view, this does not have any bearing on the question under consideration. It seems to me that this clause has been inserted in the deed in order to safeguard the interest of the vendor, who was keen to see that he would get as much as possible for the sale of the goodwill. On F the facts I am also of the opinion that the goodwill was an asset of an enduring nature. The very fact that payment was to be made over a number of years and the nature of a chartered accountant's business lead to this conclusion.

In my view, it is a very ingenious attempt to avoid payment G of tax by making it appear somehow that the payment of purchase money may be treated as payment of a royalty. In the view I take of the deed it is not necessary to discuss the numerous cases referred to by Shelat J. In my opinion, the High Court came to the correct conclusion and the appeals should be dismissed with costs.

H **Shelat, J.** Prior to November 1948, one Padamsi Haridas carried on his profession as a chartered accountant in the name

(1) [1966] 62 I.T.R. 566.

of Devidas Vithaldas and Co. By a deed of partnership, dated November 30, 1948, he took one Amratlal Parikh as a partner, reserving, however, to himself all the rights and interests in the goodwill of that business.

On January 2, 1951, he retired from the said partnership. Cl. (1) of the Deed of Dissolution executed on that occasion provided that the said partnership shall be deemed to have been dissolved as from December 31, 1950, but the business shall, as from that date, be carried on in the said name by the said Amratlal alone. Cl. (2) of the said deed ran as follows :

> "2. The goodwill of the late partnership belonged to the said Padamsi alone. He has agreed to sell the same to the said Amratlal. As consideration for and in full satisfaction of the purchase price of the goodwill of the said late partnership the said Amratlal shall—
>
> (a) pay to the said Padamsi for and during the terms of his natural life a share of eight annas in the rupee in the net profits of the said business or profession which the said Amratlal shall hereafter carry on in the said name of Devidas Vithaldas & Co.,
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> (b) on and after the death of the said Padamsi, pay to Bai Premlata, the wife of the said Padamsi, (if she be then surviving), for and during the term of her natural life a share of eight annas in the rupee in the net profits of the said business or profession which the said Amratlal shall hereafter carry on in the name of Devidas Vithaldas & Co., and
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> (c) on and after the death of the said Padamsi as well as his said wife Bai Premlata, pay to Subhas the son of the said Padamsi for and during the term of his natural life a share of eight annas in the rupee in the net profits of the said business or profession which the said Amratlal shall hereafter carry on in the name of Devidas Vithaldas & Co."

Cl. (3) provided that nothing contained in the deed shall constitute or be deemed to constitute any future partnership between the parties to the deed or between the said Amratlal and the said Bai Premlata, or the said Subhas in respect of the business to be carried on by Amratlal in the name of Devidas Vithaldas & Co. Cl. (4) declared that accounts had been made up between the parties, and that neither party had any claim against the other except as provided in said clause (2). By cl. (5) it was made clear that the said Amratlal shall henceforth remain liable for all

A the obligations and liabilities which might be incurred in respect of the said business to be carried on in the name of Devidas Vithaldas & Co., and he shall accordingly indemnify the said Padamsi against all actions, claims, demands, costs, charges and expenses whatsoever in respect of the same or in any other manner relating to the premises. Lastly, cl. (6) provided that in the B event of Amratlal transferring or assigning his said business to any person or persons, or carrying on the said business in partnership with some other person or persons, or remaining otherwise interested or concerned directly or indirectly in the business or profession of chartered accountants by whomsoever carried on in the name of Devidas Vithaldas & Co., or any other name resem- C bling or similar thereto, or in the event of any of the heirs or legal representatives or nominees of Amratlal carrying on the said business or profession in the name of Devidas Vithaldas & Co., then in any such events they and "so long as any such business be carried on in the name style and firm of Devidas Vithaldas & Co. or any other name resembling or similar thereto, the assignees of the said Amratlal and/or the said Amratlal and/or any such D other person or persons as aforesaid carrying on such business under the name style and firm of Devidas Vithaldas & Co. shall as aforesaid pay to the said Padamsi or his said wife Bai Premlata or his said son Subhas for and during the terms of their respective lives the said eight annas share in the rupee in the net profits of any such business as is hereinbefore directed to be paid by the E said Amratlal under clause 2 hereof——". The clause next provided that "the said Amratlal shall not assign or transfer or otherwise dispose of the said business or the goodwill thereof or bequeath the same to any person whomsoever nor enter into any partnership or other arrangement with any other person or persons for carrying on the said business in the said name—except F with a condition that the provisions of this Agreement shall be accepted by such person or persons or his legatees or successors or legal representatives, and with a further condition that any such person or persons or successors or legatees or legal representatives shall forthwith after being interested in any such business and whenever required by the said Padamsi or by his wife G Bai Premlata or his said son Subhas, as the case may be, enter into an agreement with any of the last three named persons, as the case may be, similar to this agreement". By his letter dated October 13, 1955, Padamsi agreed to reduce the said share of eight annas in a rupee to five annas four pies.

H Amratlal carried on the said business in the name of Devidas Vithaldas & Co. as the sole proprietor thereof till October 17, 1955. Payments made by him during this period under cls. (2) and (6) of the said deed of dissolution were added back in his

assessments as capital payments. On October 18, 1955, he entered into partnership with one Chandrakant V. Parikh. The deed of partnership executed then by him and the said Chandrakant Parikh recited that the said Amratlal till then was carrying on the business in the name of Devidas Vithaldas & Co., that the goodwill of the said business belonged solely to the said Padamsi which he, the said Amratlal, had "bought" in consideration of his agreeing to pay a share of eight annas in the rupee to Padamsi, and after him his wife and then his son as aforesaid. Cl. (5) of the deed then provided :

> "The parties hereto shall pay 0/5/4 share in profits in a rupee as and by way of purchase price of goodwill of the said firm to the said Shri Padamsi Haridas or to his wife or to his son as stated in detail hereinbefore, instead of Re. 0/8/0 share in a rupee as agreed by the party of the First Part and Shri Padamsi Haridas. The said Shri Padamsi Haridas has agreed to this reduction in his share mutually with Shri Amratlal Kashandas Parikh and Shri Chandrakant V. Parikh. After the said share of 0/5/4 in a rupee is paid up as stated above the balance of the profit and loss of the firm shall be divided in two equal proportions between the parties of the First and the Second Part."

The firm constituted under this deed paid to Bai Premlata on and after the death of Padmsi various amounts during the years 1955—1959 under the said covenants. The firm claimed that those amounts should be deducted in its assessments for those years on the ground that its income to the extent of those payments had been diverted as a result of the overriding title created by cl. (5) of the said deed of partnership. Assessments for the relevant years showed that the amounts paid to Bai Premlata were assessed as income in her assessments, so that, if the deductions claimed by the firm were not admitted the same amounts would be assessed twice over, first in the hands of Bai Premlata and then in the assessments of the firm.

The Income Tax Officer, and in appeal the A.A.C., rejected the claim for deductions holding that the said payments were capital and not revenue payments, and that the transaction evidenced by the said deed of dissolution was one of outright sale of the goodwill and the payments made thereunder were part of the purchase price.

On an appeal to the Tribunal, the Tribunal rejected the contention of the Revenue that the transaction was a sale of the goodwill in terms following :

> "It is no doubt true that clause 2 of the agreement refers to sale of goodwill and the agreed payments as

A constituting full satisfaction of the purchase consideration. If the payments are stopped, it is not stated that there will be any right of action for any definite quantified and liquidated amount. It would mean that with the stoppage of payments the assessee will only lose the right to its contact with the clientele and opportunity
B to earn profits thereafter. These considerations only go to show that in the peculiar circumstances of the case the agreement is virtually a licence granted for user of the goodwill upon payment of one-third of the net profits derived for such user ——."

C In this view the Tribunal held that the payments constituted only a fee or rent for the use of the goodwill so long as it was used and accordingly they were in the nature of revenue expenditure.

On a reference to the High Court, the High Court held that :

"On the face of the document, therefore, we cannot
D accept the contention that it was a document merely granting a licence to use the goodwill or a mere transfer of the right of user thereof. It was an outright sale of an asset of Devidas Vithaldas & Co. namely the goodwill which till then belonged to Padamsi and in which he had reserved his exclusive right at the time when he entered into partnership with Amratlal."

E In this view, the High Court answered the questions referred to it in favour of the Revenue. It was true, the High Court observed, that the Revenue had in the assessments of Bai Premlata taken the view that "Padamsi had not sold his right, title and interest in the goodwill and merely allowed the use of it for a number of years
F and since the payment was for the user of the goodwill, it could clearly be a revenue receipt in the hands of the assessee". But it added that "this was an incorrect view to take upon the facts and circumstances that have been placed before us in the present case and upon the terms of the document dated 2nd January 1951. The order clearly shows that the document dated 2nd January, 1951 was misconstrued". It is against this view that these appeals
G have been filed.

The question upon which they must turn is as to whether the payments in question made in pursuance of the transaction incorporated in the deed, dated January 2, 1951, were in the nature of revenue or capital expenditure. If they are of the former type,
H they would obviously be admissible deductions under s. 10(2) of the Income Tax Act, 1922. That question, in its turn, depends upon the true nature of the transaction as embodied in the said deed, that is, whether it was a sale of goodwill or a licence in

consideration of Amratlal and/or his assignees or transferees paying the aforesaid share until he or they used the said name. A

As has been observed in a number of decisions, it is not always easy to distinguish whether an agreement is for the payment of price in stipulated instalments or for making annual payments in the nature of income, that there is no single test of universal application for a solution of the question, and that therefore, the Court has to look not only into the document relating to the transaction, but also the surrounding circumstances to decide its true nature, the name which the parties give to it being of little consequence. This, of-course, does not mean that the legal character of the transaction which is the source of the receipt in question can be ignored and substituted by what the Taxing Authority considers the substance of the matter. The assessing authority is undoubtedly entitled and is, indeed, bound to determine the true legal relationship resulting from a transaction. If the parties have chosen to conceal, by a device, the true legal relation, it is open to it to unravel such device and to ascertain the true nature of the relationship. If the transaction is embodied in a document, the liability to tax depends upon the meaning and content of the language used in it in accordance with the ordinary rules of construction.(1) B C D

In distinguishing between capital and revenue expenditure, the courts have applied in different cases different tests. Nonetheless, it is recognised that none of them by itself is conclusive, and the determination one way or the other has to be made on the facts and circumstances of each case. E

One of the tests so applied is whether the expenditure in question was for bringing into existence an asset or an advantage of "an enduring nature".(2) and is made "once and for all", meaning thereby an expenditure made once and for all for procuring an enduring benefit. It may be payable not necessarily all at once but even by instalments as against a recurrent expenditure in the nature of operational expenses. (See *Assam Bengal Cement Co. Ltd.* v. *CIT*(3). The question in such cases would be, is the expenditure the assessee's working expenses laid out as part of the process of profit earning or a capital outlay necessary for the acquisition of a property or of rights of a permanent character, the possession of which is a condition of carrying on the trade.(4) But the expressions, 'enduring benefit'. and 'rights of a permanent F G

(1) *C.I.T.* v. *Kharwar*, [1969] 72 I.T.R. 603

(2) *Athertion* v *British Insulated Nnd Helsby Cables Ltd*, 10 T C 155

(3) 27 I T R 34, 46 H

(4) *Robert Addie and Sons, Collieres Ltd.*, v. *Commissioners of Inland Revenue*, 8 T C 671.

A nature', are only descriptive and not definitive and are relative in meaning, not synonymous with perpetual or everlasting. For instance, an expenditure incurred in common with other companies producing copper to bring down production so as to prevent a steep fall in the prices was construed to mean for one of them to be out of production for 12 months only and not for B good. On such construction, it was held that to call such an expenditure a capital expenditure would be contradiction in terms, for, it was not and was not intended to be one for acquiring a right of an enduring benefit or as an accretion to the capital or income earning structure of the business.(1) *C.I.T., West Bengal* v. *Coal Shipment (P) Ltd.*,(2) an agreement was arrived at C between two companies exporting coal to Burma. The assessee company agreed thereunder to pay, in consideration of the other company prebearing from exporting and procuring coal for its export by the assessee company, five annas per ton (subsequently raised to Rs. 1-5-0 per ton). The amounts so paid to the other company were taxed in the hands of that company. The respondent-company claimed them as admissible business expenditure D for the assessment years in question. The Revenue, on the other hand, claimed that the payments were for acquiring monopoly and were therefore not allowable as revenue expenditure. This Court upheld the assessee's contention that the expenditures were not for acquiring the monopoly, but were made to make the business more facile and profitable, that they were made as a tempo- E rary measure and not for deriving an advance of an enduring character. Observing that the agreement between the two companies was not for any fixed term and could be terminated at any time at the volition of any of the parties, it was held that although an enduring benefit need not be of an everlasting character, it should not at the same time be transitory or ephe- F meral, so that it can be terminated at any time at the volitior of either of the parties. Payments to ward off competition would constitute capital expenditure, provided the objection is to derive an advantage by eliminating the competition over some length of time but such a result would not follow if there is no certainty of duration for such an advantage and the same could be put an end to at any time. Thus, what the extent of durability or G permanence should be depends on the facts of each case.

Payments made by a lessee of a limestone quarry to the Government, who were the lessors, in consideration of a covenant which eliminated competition in the lessee's field of operations for twenty years, which was the lease period, were held to be H capital expenditure for acquiring an enduring benefit to the

(1) *Commissioners of Taxes* v. *Nchanga Consolidated Copper Mines Ltd.*, [1965] 58 I.T.R. 241.

(2) Civil Appeals Nos. 1494 to 1498 to 1971, decd on October, 14, 1971.

lessee.(1) On the other hand, registration of trade-marks under the Trade Marks Act, 1940, valid for a period of seven years only, on the expiry of which it had to be renewed by paying fresh fees, was held not to bring any enduring benefit, and therefore, the fees paid for registration were not capital but revenue expenditure.(2) Registration is only a mode of ensuring the exclusive right in a trademark, and not the acquisition of the trade-mark itself, which would be an acquisition of a capital asset. Such a distinction was made in a case where expenditure was for the renewal of a licence, which was held to be a payment made as purchase price of a monopoly for the duration of the licence, which was only for twelve months. The thing that was paid for, it was said, was a permanent quality, that is, the monopoly, although its permanence being conditioned by the renewal of the terms under which the licence was granted was shortlived. Such an expenditure was treated as of that class to which a premium on the grant of a lease belong which admittedly is not deductible, (see *Henriksen* v. *Grafton Hotel Ltd.*(3) In *Strick* v. *Regent Oil Co. Ltd.* (4) Lord Reid, however, limited the decision in *Henriksen's case*(3) to its own special facts and expressed his disagreement with it if it was to be held to have laid down any general proposition. The expression 'enduring advantage' is, thus a relative term, not enduring in the sense of its being permanent, but is sufficiently durable depending upon the nature of the terms upon which it can be acquired. So also the expression 'once and for all', which does not mean payment at one time of the whole amount, but includes payment of a lump sum, as distict from recurrent, distributed in periodic instalments.

The other test sometimes applied is payment when it is referable to fixed capital or capital assets as against payment referable to circulating capital or stock-in-trade. But this test also is not capable of being treated as of uniform application. Price paid for the acquisition of a capital asset may take sometimes the form of payments of a revenue character. The simpliest example is interest paid on the unpaid purchase price of capital asset. Though in relation to and referable to acquisition of a capital asset, it is nonetheless a revenue disbursement. On the other hand, in *Assam Bengal Cement Co.* v. *C.I.T.*(1) where the payment in question was for eliminating competition, the test of the expenditure having been incurred for and referable to a capital asset was applied.

Acquisition of the goodwill of the business is, without doubt, acquisition of a capital asset, and therefore, its purchase price

(1) 27 I.T.R. 34, 46.
(2) *C I T* v *Finlay Mills*, [1951] 20 I,T,R, 475.
(3) 24 T C 453 (4) 43 T C 1, 38

A would be capital expenditure. It would not make any difference whether it is paid in a lump sum at one time or in instalments distributed over a definite period. (see *In Re Ramjidas Jain & Co.*(1) and *Kuppuswami* v. *C.I.T.*(2) Where, however, the transaction is not for acquisition of the goodwill, but for the right to use it, the expenditure would be revenue expenditure.

B

Illustrative of such cases is the one in *Ogden* v. *Medway Cinemas Ltd.*,(3) where the respondent-company acquired by assignment the rights of the assignor under an underlease, by which he became the lessee of the cinema hall, together with the fixtures, fittings and furniture, at a yearly rent. There was also a supplemental deed by which he was granted the goodwill of C the cinema business on payment of £ 500/- per annum. The supplemental deed was to run concurrently with the underlease, that is for 13 years, and was to cease if the underlease was terminated. The deed also contained an option for the purchase of the head lease and the goodwill for £. 3,500/. The payment of £ 500/- per annum under the supplemental deed was held to be D admissible deduction. At page 695 of the report, Finlay, J., pointed out that though the deed used the expression 'grant of goodwill for a period' there was no sum mentioned as being the payment for that, followed by distribution of that sum in instalments, "but the thing is expressed to be for a payment of £ 500 per annum" without reference to any lump sum followed by a E splitting up into annual payments. "The substance of the matter here seems to me to be this—and I think it is supported by the actual language used, in particular by the expression provision contained later for the purchase in certain circumstances of the goodwill—that this is a revenue payment for the use during a certain period of certain valuable things and rights." As Lord Halsbury put it in a case where a lump sum was expressly pro- F vided for but was payable by instalments, there is an antecedent debt and the instalments are paid in liquidation of that debt. (see *The Secretary of State for India* v. *Scoble.*(4)

Another case, illustrative of such a test, is in *Jones* v. *Commissioner of Inland Revenue,*(5) where there was a sale of pro- G perty for a lump sum of £. 750, £. 300 out of which were payable by three equal instalments, and the balance of £. 450 payable by a royalty. The whole of £. 750 was treated as a capital sum, but there was a further clause "to pay by way of additional consideration a further clause of 10% upon the invoice price of all machines constructed under the said inventions and sold during the period of ten years." In respect of this latter H

(1) [1945] I T R 430.
(2) [1954] 25 I T R 349
(3) 18 T C 691.
(4) [1903] A C 299.
(5) 7 T C 310.

sum, it was held that since it was dependent on the volume of business, which rose and fell with the chances of the business, it was income and not capital, although it was actually referable to the purchase price. *In Commissioners of Inland Revenue* v. *Ramsay*,(1) the assessee purchased a dental practice for a primary price of £. 15,000. That was to be satisfied first by an immediate payment of £. 5,000 and as to the balance of £. 10,000 by payment each year, for ten years, of a sum equivalent to 25% of the net profits of the practice for each year. Such annual payment obviously might vary from time to time depending upon the quantum of business and the profits. Nevertheless, the price of £. 15,000 was not otiose, nor the balance of £. 10,000 after the initial payment of £. 5,000. The only thing that was stipulated by the parties was that the vendor was satisfied with receiving 25% of the net profits each year for the period of years, even if the actual payment turned out on the whole to be more or less than £ 15,000. As Lord Wright said, the figure of £. 15,000 "permeates the whole of the contract and upon which the whole contract depends. That being so, I think that the £. 886 in question (one of the sums equivalent to 25% of the net profits) was a sum in the nature of capital, and therefore, it was not competent for the Respondent to deduct it in returning his total income". That the sum of £. 15,000 was the lump sum purchase price was also made clear by Lord Greene when he said that a payment less than that amount could be made only if clause (4) of that agreement came into operation, that is, if the assessee continued his practice for the whole of the period of ten years. If he were to cease to practise, say after seven years, he would be liable to pay the whole of the balance of £. 15,000 then remaining due. The transaction was thus viewed as a purchase of the business for a fixed amount, payable in ten years by annual instalments, which by the mode of payment, agreed to between the parties, might at the end turn out to be more or less than the agreed purchase price of £. 15,000. Unlike *Ramsay's case*,(1) in *Vithaldas Thakordas and Co.* v. *C.I.T.*,(2) there was no fixed lump sum, nor a definite period during which payments were to be made. One Vithaldas Thakordas, who during his life-time carried on bullion business in the name of Vithaldas Thakordas & Co., died in 1930 leaving him surviving his widow Bai Tarabai. Under an arrangement made by the said Tarabai, first with five and later on with four persons, the name of Vithaldas Thakordas & Co. was used by those persons carrying on their own business in partnership. The partnership deed provided that in consideration of Bai Tarabai "having agreed to allow the partnership to use the name of Vithaldas Thakordas & Co. for the purposes of partnership", the partnership would pay out of the net profits an amount equivalent to

(1) 20 T C 79 (2) [1946] I T R 822.

A two annas in the rupee of the net profits. It also provided that after payment of the said amount out of the net profits, the balance of net profits would be divided amongst the partners according to their respective shares. No term was fixed for the duration of the use of the goodwill. Evidently, the right to use the name would cease when the partnership ceased to pay the B amount of two annas in the rupee in the partnership's net profits. On a question whether the payment was an admissible deduction, the High Court of Bombay, relying on *Ogden* v. *Medway Cinemas Ltd.*(1) held that the payment was a revenue expenditure, the transaction between the partnership and the said Bai Tarabai being not a purchase of the capital asset. It is true that the words C used in the document were such as one would find in a document of a licence. But, as already stated, it is not form but the substance of the transaction that matters. Besides, the decision did not rest on those words but on what truly the nature of the transaction was and the analogy it bore with that in *Ogden* v. *Medway Cinemas Ltd.*(1)

D A case of a similar nature is also to be found in *Travancore Sugars and Chemicals Ltd.* v. *C.I.T.*(2). There the assessee-company was floated to take over the assets of three undertakings run by Travancore Government, a sugar manufacturing concern, a distillery and a tincture factory. The first was to be purchased for Rs. 3.25 lacs, the second on a joint valuation of parties, and the third on the book value of the assets Cl. (7) of the agree-E ment provided that apart from the cash consideration the Government would be entitled to 20% of the annual net profits subject to a maximum of Rs. 40,000 after providing for depreciation and the remuneration payable to the company's treasurers and secretaries. The question was whether a sum of Rs. 42,480 paid in the previous year in question was a capital or a revenue expendi-F ture. Reversing the High Court's judgment, which held it to be a capital disbursement, this Court held that it was a revenue expenditure and gave for its decision three reasons, namely, (a) that the payment was for an indefinite period, (b) that it was related to annual profits which flowed from the trading activities and had no relation to the capital value of the assets, and (c) G that the payment was not related to, nor tied in any way to any fixed sum agreed between the parties as part of the purchase price of the three undertakings. These were also the three considerations applied by Lord Greene, M. R. in *Commissioners of Inland Revenue* v. 36/49 *Holdings Ltd.*(3)

The question whether the disbursements in question partake H the character of one or the other mainly depends upon the construction of the document of January 2, 1951 and the true nature

(1) 18 T C 691 (2) (1966) 62 I T R 566.
(3) 25 T C 173, 183

of the transaction embodied therein. Cl. (2) of the document, no doubt, uses expressions, such as "agreed to sell" and "the purchase price of the goodwill". These expressions, however, are, as repeatedly stated in a number of cases, not determinative of the exact nature of the transaction or the relationship between the parties arising therefrom. Though cl. (2) uses expressions which on a superficial view might appear to indicate a sale of the goodwill, neither that nor any other clause mentions what its purchase price was. The document is not one of those where the price is expressed at a lump sum, and is made payable by specific instalments within a specified period. In some cases, it may even be possible that parties might agree to a lump sum as the price and yet, as in *Ramsay's case,*(1) agree that such sum should be payable out of the profits at a certain percentage, where the purchaser is not in a position to pay the price at a time or even by instalments, except at a particular rate from out of the profits of the business taken over by him. But in such a case the payment, even if out of the profits, is tied up with a lump sum, that is, with the purchase price agreed to between the parties and which assumes the character of a fixed debt. Cl. (2) clearly does not fix such a price nor mention a lump sum in respect of which annual payments as provided therein are to be made.

The clause, no doubt, prescribes the mode and the quantum of the payment, that is, a share of five annas four pies in the rupee in the net profits of the business, payable during the lifetime of Padamsi and after him during the lifetime of his wife Bai Premlata if she were to survive him, and then to their son during his lifetime. Two things, however, may at once be observed, firstly, that the duration of payment is indefinite, unlike *Ramsay's case* (1) and secondly the amount is indefinite, depending as it does upon the rise and fall in the profits of the business. Obviously, the payment is not related to any lump sum fixed as the purchase price. On the contrary, it is directly related to and dependent upon whether at all and what profits are made. Further, the document is totally silent as to what is to hppen to the goodwill if Amratlal Parikh or his partners, if he were to enter into a partnership, cease to carry on the business in the name of Devidas Vithaldas & Co. or at all. It is silent as to whether the goodwill would remain with him and/or his partners, or whether it would revert to Padamsi or his heirs. The transaction thus contains all the grounds given in the case of *Travancore Sugars and Chemicals Ltd.*(2) upon which this Court concluded there that such payments could not be treated as capital disbursements, namely, an indefinite period, absence of any expressed lump sum, and payment relating to profits and not being tied up with any fixed sum agreed to as the purchase price of a capital asset.

(1) 20 T C 79. (2) 62 I.T.R. 566.

A Quite apart from these considerations, cl. (6) itself contains indications of the transaction not being an outright purchase of the goodwill. It will be recalled that that clause provides that in the event of Amratlal transferring or assigning his business to any one else or entering into partnership or otherwise remaining interested in the said business, by whomsoever carried on in the B name of Devidas Vithaldas & Co., then in any such events and "so long as any such business be carried on in the name, style and firm of Devidas Vithaldas & Co. or any other name resembling or similar thereto", the assignees of Amratlal and/or any such other person or persons as aforesaid, carrying on the business in the said name, shall pay the said share in the profits to Padamsi, fter him C to his widow and after her to his son. The clause thus indicates that the payment is to be made so long as the business is carried on in the name of Devidas Vithaldas & Co. and not otherwise. The clause further provides that the said Amratlal shall not assign or transfer or otherwise dispose of the said business or the goodwill thereof (meaning thereby the business carried on in the said name) except upon a condition that such an assignee or transferee shall D enter into a similar agreement with Padamsi or his wife or his said son, as the case may be, whensoever required to do so. When Amratlal took Chandrakant Parikh as his partner, it was in pursuance of this covenant that the deed of partnership between them expressly provided for the payment of 0/5/4 in a rupee in the net profits and further provided that it would be after such E payment was made that the partners could divide the balance left as their shares of the profits.

If the transaction embodied in the deed, dated January 2, 1951 was an outright purchase of goodwill, there was no necessity of cl. (6) in that deed providing for the partnership which Amratlal would enter into in the future or his assignee or transferee F having to pay the said share so long as he or they continued to carry on business in the said name. It is also inconceiveable that if Padamsi was selling the goodwill, he would enter into an agreement which provided no fixed purchase price, no specific period during which the purchaser would be liable to pay it except an indefinite period, *i.e.*, until the business was carried on in the G said name, leaving to the volition of the other party to use the said name or not or to cease to do so at any time. If the transaction was intended to be an outright sale of a capital asset, the deed incorporating it would have contained a fixed purchase price and even if such a fixed purchase price were to be payable not at once but by instalments, such payments would be relatable to and tied H up with such a lump sum. Even if such instalments were to be payable out of the profits of the business, such instalments would be relatable to the price, and for a period until it was satisfied and not to the profits which would fluctuate from year to year. In

such a case, even if the purchase price is payable by instalments and out of profits, the document would contain both a fixed purchase price and a definite period during which such price would have to be liquidated. A

On the facts of the case, the conclusions is inescapable, even apart from the ratio in the *Travancore Sugars and Chemicals'* case(1) being applicable, that the transaction was, as held by the Tribunal, a licence and not a sale of the goodwill. The disbursements in question, therefore, were in the nature of royalty and must be treated as admissible deductions. In this view, it does not become necessary to go into the question whether cl. (6) in the deed, dated January 2, 1951 and cl. (5) in the deed, dated October 18, 1951 contained overriding provisions by reason of which payments in question could not form part of the assessable profits of the firm. B C

The appeals are, in this view, allowed with costs, both here and in the High Court. The costs, however, will be only one set of costs. D

ORDER

In view of the decision of the majority, the appeals are allowed with costs in this Court and in the High Court. One set of costs.

(1) 62 I T R 566.