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

+ **INCOME TAX APPEAL NO. 70/2013**

% Date of decision: 15th November, 2018

COMMISSIONER OF INCOME TAX-III Appellant
Through: Mr. Asheesh Jain, Sr. Standing Counsel
with Mr. Sanjay Kumar, Advocate.
versus

SHYAM TELELINK LTD. Respondent
Through: Mr. Piyush Kaushik, Advocate.

INCOME TAX APPEAL NO. 73/2013

COMMISSIONER OF INCOME TAX-III Appellant
Through: Mr. Asheesh Jain, Sr. Standing Counsel
with Mr. Sanjay Kumar, Advocate.
versus

SHYAM TELELINK LTD. Respondent
Through: Mr. Piyush Kaushik, Advocate.

INCOME TAX APPEAL NO.1069/2017

PR. COMMISSIONER OF INCOME TAX-8 Appellant
Through: Mr. Asheesh Jain, Sr. Standing Counsel
with Mr. Sanjay Kumar, Advocate.
versus

SISTEMA SHYAM TELESERVICES LTD. Respondent
Through: Mr. Piyush Kaushik, Advocate.

CORAM:
HON'BLE MR. JUSTICE SANJIV KHANNA
HON'BLE MR. JUSTICE ANUP JAIRAM BHAMBHANI

SANJIV KHANNA, J.

These appeals by the Revenue under Section 260A of the Income Tax Act, 1961 (Act, for short) in the case of Sistema Shyam Teleservices Ltd., formerly known as Shyam Telelink Ltd., relate to Assessment Years 2003-04, 2004-05 and 2009-10.

2. As a similar and identical issue arises for consideration, these appeals are being disposed of by this common order.
3. The substantial question of law framed in these appeals reads as under:-

“Whether on the facts and in the circumstances of the case the Tribunal erred in holding that the amount received on sale of prepaid cards to the extent of unutilized talk time did not accrue as income in the year of sale? ”

4. In view of the limited controversy which relates to the year of taxability of the prepaid cards we need not refer to the assessment order and the appellate orders in each case.
5. Respondent-assessee was engaged in the business of providing basic telecom services in the State of Rajasthan and had both prepaid and postpaid subscribers. Postpaid customers were billed on the basis of actual talk time. There is no dispute regarding year of taxability of the postpaid customers.

The dispute raised in the present appeals pertains to accounting treatment in respect of prepaid cards. As per the Revenue, the respondent-assessee must account for and include the entire amount paid on the date of purchase of the prepaid card by the subscriber. Date of purchase of the prepaid card would be the date when income had accrued to the respondent-assessee. The respondent-assessee, however, recognizes revenue on prepaid cards on the basis of actual usage. In other words, unutilized amount outstanding on the prepaid card, if any, at the end of the financial year, was carried forward to the next year. The unutilized amount on the prepaid card was treated as advance in the balance-sheet and recognized as a revenue receipt in the subsequent year, when the talk time was actually used or was exhausted when the card lapsed on expiry of the stipulated time.

6. Learned counsel for the respondent-assessee has rightly submitted that the contention of the Revenue even if accepted would be revenue neutral, since the addition made in the first year will result in correspondingly reduction in the revenue of the next year and so on and so forth. Revenue while not disputing the submission, submits that the respondent-assessee must duly account for the entire unutilized amount in the next year. On the said aspect, learned counsel for the respondent-assessee has drawn our attention to paragraph 16 of the order dated 9th July, 2012 passed by the Income Tax Appellate Tribunal ('Tribunal', for short) for the Assessment Years 2003-04 and 2004-05 by which the matter has been restored to the file of the Assessing Officer to verify and ascertain whether there was any revenue leakage. We find that the aforesaid submission made by the

respondent-assessee is correct. For clarity, we would like to reproduce paragraph 16 of order dated 9th July, 2012, which reads:-

“In the present case, the main dispute is regarding revenue recognition relating to unused talk time remaining available as at the end of the year. As noted earlier, there is no dispute that company had to provide talk time to its subscriber till the expiry of the period of card or till complete utilization of talk time, whichever is earlier. As long as assessee company is under obligation to provide talk time, it cannot be said that a debt has accrued in favour of assessee company against the subscriber. The assessee company cannot appropriate the charges relating to available talk time to the exclusion of subscriber as long as it is under obligation to provide the said services. Therefore, we are of the opinion that Id. CIT (A) in principle has rightly accepted the mode of revenue recognition by assessee. Ld. DR has submitted that from the system followed by the assessee, there is every likelihood of revenue leakage. In this regard Id. Counsel has submitted that the matter can be restored to the file of AO for verification of this aspect only. We, therefore, restore the matter to the file of AO for the limited purpose of verification whether in the subsequent year the assessee has declared the revenue in respect of expired pre-paid cards or not. In case no discrepancy is found in this regard, no adjustment is called for with the assessee’s mode of revenue recognition. In terms of aforementioned observation this ground is partly allowed for statistical purposes.”

7. Learned counsel for the respondent-assessee submits that the Revenue has accepted similar directions passed by the Tribunal for Assessment Years 2010-11 onwards. Learned counsel for the Revenue is unable to controvert the submission in the absence of instructions. Revenue it appears has not

taken a consistent stand on the question of year of taxability of a particular receipt. Counsel for the respondent-assessee has also submitted that the Assessing Officer while making the addition in one year did not correspondingly reduce the receipt by a similar amount in the next/succeeding year. Counsel for the Revenue is unable to controvert or deny the said position, albeit he states that the respondent-assessee had not made any such claim in the return. Be that as it may, the Assessing Officer while making addition in one year in respect of receipt which was accounted for in the next year should pass a consequential order to ensure that the income or receipt is not taxed twice.

8. Quantum or revenue earned would be income in one year or the other year. Counsel for the respondent-assessee had drawn our attention to tables/chart filed before us. Rs.44,42,221/- added to the income of the Assessment Year 2003-04 was required to be reduced from the receipts shown by the respondent-assessee in the Assessment Year 2004-05. Similarly, addition of Rs.72,64,139/- made in the Assessment Year 2004-05 has to be reduced from the income in the Assessment Year 2005-06. In fact, the income for the Assessment Year 2005-06 would be lower as the carried-forward talk time of Rs.30,74,152/- was lower than the talk time of Rs.72,64,139/- carried-forward from the Assessment Year 2004-05. In the Assessment Year 2009-10 the carry-forward talk time taxed by the Assessing Officer was Rs.7,65,19,216/-. This amount has to be reduced from the revenue receipts for the assessment year 2010-11. The amount carried-forward to the assessment year 2011-12 was Rs.34,88,62,307/-. This would possibly explain the reason why the Revenue has not filed any appeal against the order

of the Tribunal for the Assessment Year 2011-12 onwards. If the stand of the Revenue is to be accepted, then the receipts of the respondent-assessee to the tune of Rs.34,88,62,307/- have to be reduced in the next assessment year 2011-12.

9. However, we would not like to dispose of the present appeals only on the aforesaid basis, for we find that there is merit in the findings recorded by the Tribunal, accepting the method of accounting followed by the respondent-assessee. The Tribunal in the impugned order has referred to the difference between receipt of an amount and accrual of income. Every receipt is not income, for income is something which the assessee is legally entitled to appropriate to the exclusion of the giver. However, contention of the Revenue that the prepaid amount once paid and received by the assessee was forgone by the subscriber and accordingly appropriated by the respondent-assessee is substantially correct. At the same time, the payment was an advance and was subject to the respondent-assessee providing basic telecom service as promised, failing which the unutilized amount was required to be refunded to the pre-paid subscribers.

10. The respondent-assessee states that they have been following the principles of Revenue Recognition as per Accounting Standards. Paragraph 7 of Accounting Standards stipulates:-

“7. Rendering of Services

7.1 Revenue from service transactions is usually recognised as the service is performed, either by the proportionate completion method or by the completed service contract method.

(i) Proportionate completion method—Performance consists of the execution of more than one act. Revenue is recognised proportionately by reference to the performance of each act. The revenue recognised under this method would be determined on the basis of contract value, associated costs, number of acts or other suitable basis. For practical purposes, when services are provided by an indeterminate number of acts over a specific period of time, revenue is recognised on a straight line basis over the specific period unless there is evidence that some other method better represents the pattern of performance.

(ii) Completed service contract method—Performance consists of the execution of a single act. Alternatively, services are performed in more than a single act, and the services yet to be performed are so significant in relation to the transaction taken as a whole that performance cannot be deemed to have been completed until the execution of those acts. The completed service contract method is relevant to these patterns of performance and accordingly revenue is recognised when the sole or final act takes place and the service becomes chargeable.”

Paragraph 7 stipulates that revenue from service transaction can be recognized either by proportionate completion method or by the completed service contract method. Revenue is generally recognized when the service is performed. Proportionate completion method is a recognized accounting method, as per which revenue is recognized proportionately by reference to the performance of each act. Under this method, revenue is determined on the basis of contract value, associated costs, number of acts or other suitable criteria. In other words, when services are provided by an indeterminate number of acts over a specific period of time, revenue is recognized on a straight line basis over the specific period. This is subject

to any evidence that some other method would be better and more appropriate for representing the pattern of performance.

11. A Division Bench of Delhi High Court had occasion to deal with Accounting Standard 9 in *Commissioner of Income-Tax Vs. Dinesh Kumar Goel* [2011] 331 ITR 10 (Del). This was a case of a coaching institute that had received entire fee for the course spread over two years' duration at the time of admission of the students. However, the entire fee was not accounted in the year of receipt when the entire payment was made, but was spread over the entire duration of the course and accordingly accounted in the books of accounts and income tax returns. We would clarify that the assessee therein was following mercantile system of accounting. Reference was made to *E.D. Sassoon and Co. Ltd. Vs Commissioner of Income Tax* [1954] 26 ITR 27 (SC) to observe as under:-

“12. Section 5 of the Act gives the “scope of total income”. Sub-Section (1) thereof, with which we are concerned, reads as under:

“(1) Subject to the provisions of this Act, the total income of any previous year of a person who is a resident includes all income from whatever source derived which

(a) Is received or is deemed to be received in India in such year by or on behalf of such person; or

(b) Accrues or arises or is deemed to accrue or arise to him in India during such year; or

(c) Accrues or arises to him outside India during such year.”

13. As is clear from reading of Clause (b) above, even when the income accrues or arises or is deemed to accrue or arise to the assessee in India during previous year, that is to be taxed in that year. It is important, therefore, that receipt of a particular amount in the relevant year should be an “income” under the aforesaid provision. What is the relevant yardstick is the time of accrual or arisal for the purpose of its taxation, viz., in order to be chargeable, the income should accrue or arise to the assessee during the previous year. If income has accrued or arisen, even if actual receipt of the amount is not there, it would be chargeable to tax in the said year. Though the amount may be received later in the succeeding year, the income would be said to accrue or arise if there is a debt owed to the assessee by somebody at that moment. From this, it follows that there must be the “right to receive the income on a particular date, so as to bring about a creditor and debtor relationship on the relevant date”. The Court further explained that a right to receive a particular sum under the agreement would not be sufficient unless the right accrued by rendering of services and not by promising for services and where the right to receive is anterior to rendering of service, the income, therefore, would accrue on rendering of services. Following discussion in this judgment would demonstrate the principle which we have highlighted above:

“37. Mukerji J. has defined these terms in *Rogers Pyatt Shellac & Co. v. Secretary of State for India* 1 I.T.C. 363:

"Now what is income? The term is nowhere defined in the Act..... In the absence of a statutory definition we must take its ordinary dictionary meaning - 'that which comes in as the periodical produce of one's work, business, lands or investments (considered in reference to its amount and commonly expressed in terms of money);

annual or periodical receipts accruing to a person or corporation" (Oxford Dictionary). The word clearly implies the ideal of receipt, actual or constructive. The policy of the Act is to make the amount taxable when it is paid or received either actually or constructively. 'Accrues,' 'arises' and 'is received' are three distinct terms. So far as receiving of income is concerned there can be no difficulty; it conveys a clear and definite meaning, and I can think of no expression which makes its meaning plainer than the word 'receiving' itself. The words 'accrue' and 'arise' also are not defined in the Act. The ordinary dictionary meanings of these words have got to be taken as the meanings attaching to them. 'Accruing' is synonymous with 'arising' in the sense of springing as a natural growth or result. The three expressions 'accrues,' 'arises' and 'is received' having been used in the section, strictly speaking 'accrues' should not be taken as synonymous with 'arises' but in the distinct sense of growing up by way of addition or increase or as an accession or advantage; while the word 'arises' means comes into existence or notice or presents itself. The former connotes the idea of a growth or accumulation and the latter of the growth or accumulation with a tangible shape so as to be receivable. It is difficult to say that this distinction has been throughout maintained in the Act and perhaps the two words seem to denote the same idea or ideas very similar, and the difference only lies in this that one is more appropriate than the other when applied to particular cases. It is clear, however, as pointed out by Fry L.J. in *Colquhoun v. Brooks* (1888) 21 Q.B.D. 52, 59 [this part of the decision not having been affected by the reversal of the decision by the House of Lords (1889) 14 App. Cas. 493 that both the words are used in

contradistinction to the word "receive" and indicate a right to receive. They represent a stage anterior to the point of time when the income becomes receivable and connote a character of the income which is more or less inchoate.

One other matter need be referred to in connection with the section. What is sought to be taxed must be income and it cannot be taxed unless it has arrived at a stage when it can be called 'income.'

38. The observations of Lord Justice Fry quoted above by Mr. Mukerji J. were made in *Colquhoun v. Brooks* (1888) 21 Q.B.D. 52 while construing the provisions of 16 and 17 Victoria Chapter 34 section 2 schedule 'D'. The words to be construed there were 'profits or gains, arising or accruing,' and it was observed by Lord Justice Fry at page 59 :

"In the first place, I would observe that the tax is in respect of 'profits or gains arising or accruing.' I cannot read those words as meaning 'received by.' If the enactments were limited to profits and gains 'received by' the person to be charged, that limitation would apply as much to all Her Majesty's subjects as to foreigners residing in this county. The result would be that no Income-tax would be payable upon profits which accrued but which were not actually received, although profits might have been earned in the kingdom and might have accrued in the kingdom. I think, therefore, that the words 'arising or accruing' are general words descriptive of a right to receive profits."

39. To the same effect are the observations of Satyanarayana Rao J. in *Commissioner of Income-tax, Madras v. Anamallais Timber Trust Ltd.*

[1950]18ITR333(Mad) and Mukherjea J. in Commissioner of Income-tax, Bombay v. Ahmedbhai Umarbhai & Co., Bombay [1950]18ITR472(SC) where this passage from the Judgment of Mukerji J. in Rogers Pyatt Shellac & Co. v. Secretary of State for India 1 I.T.C. 363 , is approved and adopted. It is clear therefore that income may accrue to an assessee without the actual receipt of the same. If the assessee acquires a right to receive the income, the income can be said to have accrued to him though it may be received later on its being ascertained. The basic conception is that he must have acquired a right to receive the income. There must be a debt owed to him by somebody. There must be as is otherwise expressed debitum in presenti, solvendum in future; See W. S. Try Ltd. v. Johnson (Inspector of Taxes) [1946]1 A.E.R. 532 , and Webb v. Stenton and Others, Garnishees 11 Q.B.D. 518 . Unless and until there is created in favour of the assessee a debt due by somebody it cannot be said that he has acquired a right to receive the income or that income had accrued to him.”

12. The argument of the Revenue that as per the agreements signed by the students, they were called upon and were required to pay the entire fee upfront for the entire course at the time of admission and, therefore, the assessee had earned full fee at that stage itself was rejected observing and referring to the principle of law laid down in *E.D. Sassoon and Co. Ltd.* (supra) that fee was debt due at the time of deposit. The fee was paid in advance though services were yet to be rendered. Reference was made to *Calcutta Company Ltd. Vs. Commissioner of Income Tax* [1959] 37 ITR 1 (SC) that when the fee was paid in advance it would be in nature of deposit or

an advance. Otherwise, it would lead to an anomalous situation not intended in law, as when the amount was received the expenses to be deducted to arrive at the net income were yet to be incurred, and would be incurred in the next financial year. The following principle was enunciated by the Supreme Court in *Calcutta Company Ltd.* (supra):-

“The expression “profits or gains” in section 10(1) of the Income-tax Act has to be understood in its commercial sense and there can be no computation of such profits and gains until the expenditure which is necessary for the purpose of earning the receipts is deducted therefrom – whether the expenditure is actually incurred or the liability in respect thereof has accrued even though it may have to be discharged at some future date.””

13. In other words, principle of matching between the revenue receipt and the expenditure to be incurred was applied. Reference was also made to the judgment of the Supreme Court in *Commissioner of Income Tax Vs. Bilahari Investment (P) Ltd.* [2008] 299 ITR 1 (SC), wherein referring to the concept of matching it was observed:-

“82. Matching Concept is based on the accounting period concept. The paramount object of running a business is to earn profit. In order to ascertain the profit made by the business during a period, it is necessary that "revenues" of the period should be matched with the costs (expenses) of that period. In other words, income made by the business during a period can be measured only with the revenue earned during a period is compared with the expenditure incurred for earning that revenue. However, in cases of mergers and acquisitions, companies sometimes undertake to defer revenue expenditure over future years which brings in the concept of Deferred Tax

Accounting. Therefore, today it cannot be said that the concept of accrual is limited to one year.

83. It is a principle of recognizing costs (expenses) against revenues or against the relevant time period in order to determine the periodic income. This principle is an important component of accrual basis of accounting. As stated above, the object of AS 22 is to reconcile the matching principle with the Fair Valuation Principles. It may be noted that recognition, measurement and disclosure of various items of income, expenses, assets and liabilities is done only by Accounting Standards and not by provisions of the Companies Act.”

14. On the question of application of the accounting principles, Section 145 of the Act and mandate of the Companies Act and paragraph 9 of the Accounting Standards, in *Dinesh Kumar Goel* (supra) it was observed:-

“28. Reading of the aforesaid (AS) 9 makes it clear that revenue is recognized only when the services are actually rendered. If the services are rendered partially, revenue is to be shown proportionate with the degree of completion of the services. This really clinches the issue in favour of the assessee.

29. Though our discussion on the issue is complete, the parting comments need to be made. The receipts relate to the unexecuted packages, which are not shown in the instant year would be shown in the succeeding year. Rate of tax in respect of companies remains the same in all these years. Therefore, the Revenue does not lose anything, as it would receive the tax on this income in the succeeding year. Still issues are raised and much outcry is made for nothing.”

15. Thereafter, the Delhi High Court in *Dinesh Kumar Goel* (supra) had quoted the following passage from the decision of Bombay High Court in *Commissioner of Income Tax Vs. Nagri Mills Co. Ltd.* [1958] 33 ITR 681 (Bom) :-

“We have often wondered why the Income tax authorities, in a matter such as this where the deduction is obviously a permissible deduction under the income tax Act, raise disputes as to the year in which the deduction should be allowed. The question as to the year in which a deduction is allowable may be material when the rate of tax chargeable on the assessee in two different years is different; but in the case of income of a company, tax is attracted at a uniform rate, and whether the deduction in respect of bonus was granted in the assessment year 1952-53 or in the assessment year corresponding to the accounting year 1952, that is in the assessment year 1953-54, should be a matter of no consequence to the Department; and one should have thought that the Department would not fritter away its energies in fighting matters of this kind. But, obviously, judging from the references that come up to us every now and then, the Department appears to delight in raising points of this character which do not affect the taxability of the assessee or the tax that the Department is likely to collect from him whether in one year or the other.”

16. In *Bilahari Investment (P) Ltd.* (supra), the Supreme Court had elucidated that revenue recognition was attainable by several methods of accounting. The same result could be attained by any one of the accounting methods. Completed contract method was one such method. Similarly, percentage of completion method was another such method. Percentage of completion method tries to attain periodic recognition of income in order to

reflect current performance. The amount of revenue recognized under this method is determined by reference to the stage of completion of the contract.

17. The appropriation of prepaid amount was contingent upon the respondent-assessee performing its obligation and rendering services to the prepaid customers as per the terms. If the respondent-assessee had failed to perform the services as promised, it would be liable and under an obligation to refund the advance payment received under the ordinary law of contract or special enactments, like the Consumer Protection Act. The aforesaid legal position would meet the argument of the Revenue that the prepaid amount received was not liable to be refunded or repaid, whether or not any services were rendered.

18. In *J.K. Industries Ltd. and Anr. Vs. Union of India and Ors.* [2008] 297 ITR 176 (SC) and *Commissioner of Income Tax Vs. Woodward Governor India P. Ltd.* [2009] 312 ITR 254 (SC), the Supreme Court has emphasized that the accounting standards as framed and followed by the auditors should be respected, for they provide harmonization of concepts and accounting principles and ensure discipline. Accounting methods followed continuously by the assessee for given period of time would ensure revenue neutrality and reflect true and correct income or profits.

19. Counsel for the Revenue has submitted that in some cases the prepaid cards would have lapsed and the subscribers may not have utilized or availed of services/talk time. Unutilized amount when the prepaid card lapses has to be treated as income or receipt of the respondent-assessee on the date when the card had lapsed. The respondent-assessee has accepted this position.

Assessing Officer would be accordingly entitled to examine this aspect when passing the appeal effect order.

20. Looked at from all angles, we do not find any reason or good ground to interfere with the order passed by the Tribunal. The substantial question of law is accordingly answered in favour of the respondent-assessee and against the Revenue. The appeals are disposed of. We would clarify that the Assessing Officer while passing the appeal effect order, would ensure that the unutilized talk time has been accounted for and included in the receipt of the year in which the amount had lapsed and was forgone. In the facts of the present case, there would be no order as to costs.

SANJIV KHANNA, J.

ANUP JAIRAM BHAMBHANI, J.

NOVEMBER 15, 2018

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