



# Supreme Court's Ruling Imposes Capital Taxation on Telecoms

**For Prelims:** Capital Expenditure and Revenue Expenditure, [Department of Telecommunication](#), Telecom Licence Fee, Amortization

**For Mains:** Difference Between Capital and Revenue Expenditure, Mobilization of Resources

[Source: IE](#)

## Why in News?

Recently, the [Supreme Court \(SC\)](#) has held that payment of **entry fee as well as variable annual license fee made by telcos** will be considered **capital expenditure and not revenue expenditure**, and taxed accordingly.

## What are the Impacts of the SC's Ruling over Telecom Licence Fee?

### ▪ Ruling:

- The **SC's** judgment stipulates that the payments made by telecom companies to the [Department of Telecommunication](#) as entry fees and annual license fees under the **(New Telecom) Policy of 1999** are now categorized as **capital expenditures** and may be **amortised** in accordance with **Section 35ABB of the (Income Tax) Act**.
  - This means that **instead of deducting the entire expenditure all at once**, the company will need to deduct a portion of the total fee over each year for tax purposes.

### ▪ Impact:

- **Change in Accounting Treatment:** Telecom companies have traditionally **treated license fees as expenses**, allowing them to **claim deductions on a year-to-date basis for tax calculations**.
  - However, this ruling mandates a shift in the accounting treatment, requiring license fees to be considered as capital expenses.
  - These expenses must be **amortized over the license's holding period**.
- **Initial Impact on Cash Flow:** As a direct consequence of the change in accounting treatment, telecom companies may experience a temporary reduction in cash flow.
  - Higher **EBITDA (Earnings Before Interest, Taxes, Depreciation, and Amortization) and PBT (Profit Before Tax)** may result from this shift, but it is likely to be offset over the license's duration.
- **Financial Strain:** The ruling is expected to affect companies that have **incurred substantial expenses to obtain telecom licenses**, particularly those already experiencing financial losses.
- **Uncertainty About Retrospective Application:** The **Supreme Court's order did not explicitly address** whether the new accounting structure should be applied **retrospectively**.

- This has raised concerns within the telecom industry, as well as questions regarding tax liabilities for prior periods.

## What is Amortization?

- It is an **accounting process** used to spread the cost of an **intangible asset or a capital expense** over its useful life.
  - This gradual allocation of expenses helps match the cost of the asset with the revenue it generates over time.
- In simpler terms, it **means dividing a large expense into smaller portions and recognizing those portions as expenses** on financial statements over a specific period.
  - This practice ensures a **more accurate representation of the asset's impact on a company's financial statements** and tax liability over time.

## What is the Difference Between Capital and Revenue Expenditure?

Aspect	Capital Expenditure	Revenue Expenditure
<b>Nature of Expenses</b>	Expenses related to <b>acquiring, improving, or extending long-term assets</b> or investments expected to benefit for more than one financial year.	<b>Day-to-day operational expenses</b> incurred for maintaining and supporting existing assets or services.
<b>Accounting Treatment</b>	<b>Capitalized on the balance sheet</b> and recognized over time through amortization or depreciation.	Fully <b>recognized as expenses</b> in the year incurred on the income statement.
<b>Tax Treatment</b>	Subject to <b>depreciation or amortization</b> , leading to a delayed tax impact and often lower taxable income in the year of purchase.	Immediately <b>deductible from taxable income</b> , providing an immediate reduction in tax liability.
<b>Impact on Profitability</b>	Generally <b>does not significantly impact short-term profitability</b> as costs are spread over several years.	Has an <b>immediate impact on profitability</b> , as expenses are fully recognized in the year incurred.
<b>Examples</b>	Acquiring a <b>new manufacturing facility</b> , research and development for a new product, long-term license or franchise.	<b>Routine machinery maintenance</b> , employee salaries, advertising costs, utility bills.

## UPSC Civil Services Examination Previous Year Question (PYQ)

### Prelims:

**Q. Which of the following is/are included in the capital budget of the Government of India? (2016)**

1. Expenditure on acquisition of assets like roads, buildings, machinery, etc.
2. Loans received from foreign governments
3. Loans and advances granted to the States and Union Territories

**Select the correct answer using the code given below:**

- (a) 1 only  
 (b) 2 and 3 only  
 (c) 1 and 3 only  
 (d) 1, 2 and 3

**Ans: (d)**

**Mains:**

**Q.** Distinguish between Capital Budget and Revenue Budget. Explain the components of both these Budgets. **(2021)**

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