



Annual franchise fees paid to BCCI to operate and participate in IPL are allowed as revenue expenditure

Background

Recently, the Mumbai Bench of the Income-tax Appellate Tribunal (the Tribunal) in the case of Knight Riders Sports Private Limited¹ (the taxpayer) held that annual payment of the franchise fees paid to BCCI to operate and participate in Indian Premier League (IPL) are deductible as revenue expenditure under the Income-tax Act, 1961 (the Act). The Tribunal observed that the payment of franchise fees has only facilitated participation in the IPL and operation of the team for the year. It did not result in the creation of an asset nor in the generation of a benefit of an enduring nature.

Facts of the case

- The taxpayer is a 100 per cent subsidiary of Red Chillies Entertainment Pvt. Limited, an Indian company, had entered into an IPL franchise agreement with the Board of Cricket Control of India (BCCI) for franchise rights of an IPL team with the home ground at Eden Garden, Kolkata. In terms of the agreement, the taxpayer was vested with the right to operate the franchise, be a member of IPL, operate a team and participate in the tournament.
- Under the terms of the agreement, the taxpayer was to pay to BCCI certain amounts, viz. (i) a 'franchisee fee' of INR300 million to be paid in 10 equal installments, and (ii) 20 per cent of sums received by each franchisee from the exploitation of the central rights and franchise rights every year from the eleventh year onward for the term of the league.

- The taxpayer claimed the franchise fees as revenue expenditure. Additionally, the taxpayer also claimed various other expenditure i.e., security charges, payment to cricket coach, food and beverages charges, travelling expenses, etc., while computing its taxable income.
- The Assessing Officer (AO) held that the franchise fee was a part of the consideration which was paid by the taxpayer for owning the IPL team and not as a fee for playing the IPL matches vested an enduring benefit with the taxpayer, therefore, the same being a capital expenditure. Further, the AO considered the franchise fees as an intangible asset and allowed depreciation at 25 per cent.
- The AO also disputed deduction of certain expenditure which did not accrue in the year and hence, was against the matching principle in the mercantile system of accounting followed by the taxpayer. The AO disallowed various other expenditure² contending that the said expenditure being of a personal nature and not related to the business of the taxpayer.
- The Commissioner of Income-tax (Appeals) [CIT(A)] upheld the AO's order.

Tribunal's decision

Characterisation of franchise fees

- The Tribunal observed that the payment of the franchise fee by the taxpayer for a year, therein vested with him a right to participate in the tournament for the said year without guarantee

² i.e. security charges, payment to cricket coach, food and beverages charges, travelling expenses, etc.

¹ Knight Riders Sports Private Limited v. ACIT (ITA No. 1307/Mum/2013) – Taxsutra.com

that in the future years it would be eligible to participate in the tournament. The payment of the franchise fee by the taxpayer as per the terms contemplated in the franchise agreement enabled it to participate in the tournament for the subject year and earn revenue from the same.

- The payment of the franchise fee by the taxpayer was in the nature of recurring annual payment which was paid to facilitate participation in the league and operating the team only for the year for which the payment pertained, with neither vesting of any right of participation in the subsequent years, nor leading to creation/ownership of an asset or generation of a benefit of an enduring nature in the hands of the taxpayer.
- The Tribunal observed that the taxpayer was not vested with any right to assign or delegate the performance of any right or obligation under the agreement. In case of breach by the franchisee of the terms contemplating the payment obligation to BCCI, the same was to be construed as a material breach of the agreement. The rights granted to the franchisee were personal to the franchisee and not right to assign the agreement or to sub-contract or otherwise delegate the franchisee's obligations under it without the BCCI-IPL written consent.
- As the aforesaid payment of franchise fee which facilitated the participation in the league and operating the team was restricted only to the year to which the payment pertained, it can be concluded that by making such payment there was neither a creation of an asset or generation of a benefit of an enduring nature in the hands of the taxpayer.
- The Supreme Court decisions relied on by the tax department in the cases of Techno Shares and Stocks Ltd.³, and Jonas Woodhead and Sons Ltd.⁴ are distinguishable to the facts of the present case.
- In view of the above observations and the decisions of the Tribunal⁵, the franchise fees are in the nature of revenue expenditure and, hence, the issue of allowance of depreciation on the payment of franchise fees, by considering the franchise fee as an intangible asset, is rendered redundant.

Allowance of franchisee fees for the next year on accrual basis

- In computing the income for the Assessment Year 2009-10, the taxpayer claimed a proportionate deduction of franchise fees amounting to INR75 million on an accrual basis (i.e., from January 2009–March 2009), which pertained to the upcoming IPL season which was to be played post March 2009.

- The Tribunal observed that the liability to make payment of the franchise fees related to the date on which the first match of the IPL was played. Since no match was played during AY 2009-10, no part of the franchise fees could be related to and characterised as expenditure during the year under consideration.
- The Tribunal held that even though the taxpayer followed the mercantile system of accounting, as no part of the franchise fees accrued or crystallised during the tax year under consideration (FY 2008-09), no part of the franchise fees could be claimed as a deduction.

Allowance of other expenditure

- The Tribunal also allowed certain other expenditure, such as amounts paid to the police welfare fund and the cricket coach, boarding, lodging expenditure, airfare travelling expenditure, vehicle hire charges and security charges of guests and celebrities, on the ground that such charges were incurred for the purpose of the taxpayer's business and, hence, allowable as revenue expenditure.

Our comments

With respect to allowability of franchise fees, the Delhi High Court in the case of Jubilant Foodwork (P.) Ltd.⁶ held that annual franchise fees paid at a fixed percentage for using a trademark belonging to the payee company should be allowed as revenue expenditure.

In the present case, the Mumbai Tribunal on perusal of the franchise agreement observed that the franchise fees were paid to facilitate participation in IPL and operating the team only for the year. It has neither vested any right of participation in the subsequent years nor created/owned an asset or generated any benefit of an enduring nature in the hands of the taxpayer. Therefore, franchise fees are in the nature of revenue expenditure.

³ Techno Shares & Stocks Ltd. & Ors. v. CIT [2010] 327 ITR 323 (SC)

⁴ Jonas Woodhead And Sons (India) Ltd. v. CIT [1997] 224 ITR 342 (SC)

⁵ India Win Sports Pvt. Ltd. v. ACIT [ITA No. 5290 & 5291/Mum/2014], DCIT v. Deccan Chargers Sporting Ventures [ITA No. 1043/Hyd/2013, 28 October 2015], and ACIT v. India Cement Ltd. [ITA No. 1342/Mds/2010, 1 January 2016]

⁶ CIT v. Jubilant Foodwork (P.) Ltd. [2014] 271 CTR 227 (Del)

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