IN THE CUSTOMS, EXCISE & SERVICE TAX APPELLATE TRIBUNAL, CHENNAI

REGIONAL BENCH - COURT NO. – III

Customs Appeal No.42109 of 2014

(Arising out of Order-in-Appeal C. Cus. No.1105/2014 dated 30.6.2014 passed by the Commissioner of Customs (Appeals), Chennai)

M/s. Dymos Lear Automotive India Pvt. Ltd. **Appellant**
Plot No. A6 & A7, SIPCOt Industrial Park
Irungattukottai
Sriperumbudur Taluk
Kancheepuram – 602 117.

Vs.

Commissioner of Customs **Respondent**
Seaport - Import
Custom House
No. 60, Rajaji Salai
Chennai – 600001.

APPEARANCE:

Shri R. Parthasarathy, Advocate for the Appellant
Shri Arul C. Durairaj, Superintendent (AR) for the Respondent

CORAM

Hon'ble Ms. Sulekha Beevi C.S., Member (Judicial)
Hon'ble Shri P. Anjani Kumar, Member (Technical)

Final Order No. **41257 / 2020**

Date of Hearing: 29.10.2020
Date of Decision: 29.10.2020

Per Ms. Sulekha Beevi C.S.

The appellants are aggrieved by the order passed by the Commissioner of Customs (Appeals) who upheld the order of the original authority directing loading of royalty charges and technical assistance fee to the assessable value for payment of duty.

2. On behalf of the appellant, ld. counsel Shri R. Parthasarathy appeared and argued the matter. The ld. AR Shri Arul C. Durairaj appeared and argued for the respondent.

3. The argument on behalf of the appellant can be summarized as under:-

3.1 The appellant is an Indian company engaged in the manufacture of "Automotive Seating Systems". Some of the components required for the manufacture of the finished goods are imported both from related and unrelated suppliers. The appellant ad entered into various Technical License and Assistance Agreement (TLAA) during the years 2008, 2011 and 2012 with their principals M/s. Dymos Inc. (name subsequently changed to M/s. Hyundai Dymos Inc.) for the manufacture of car seating system for various models of the cars manufactured by M/s. Hyundai Motors India Ltd. In terms of the said TLAA, the appellant was granted non-transferable and non-exclusive right and license to use the intellectual property rights and technical information to manufacture the automotive seating systems, on payment of running royalty as specified in the said agreements. The running royalty payable as per the 2008 agreement was 5% on the domestic sales of the product and 8% on the export sales of the product and the running royalty will be calculated on the basis of the net ex-factory sale price of the product, exclusive of excise duties minus cost of the standard bought-out components and the landed cost of imported components, irrespective of the source of procurement, including ocean freight, insurance, customs duties etc. In the 2011 agreement, the running royalty payable was redetermined at 1.6% of the gross sales of the product and as per the 2012 agreement, the running royalty payable is 2% of the gross sales of the product. The royalty rate was simply changed from a higher percentage (5%) of the net sales value to a lower percentage (1.6% / 2%) of the gross value. The payment is a condition of both manufacture and subsequent sale. It was not a condition of sale of the components imported from the related party. The appellant had also entered into a Management Consultancy Agreement (MCA) dated 1.4.2008 with M/s. Dymos Inc. The MCA inter alia provided for technical assistance by way of qualified engineers / technicians who would be made available on request of and at the expense of the appellant. The service fees payable for such assistance by the appellant is on a per diem basis for the manpower deputed by M/s. Dymos Inc. Subsequent to the change in its constitution, the appellant entered into a fresh MCA dated 28.10.2020 with M/s. Dymos Inc. as per the same terms and conditions. Since the imports were from related parties, the issue was examined by the Special Valuation Branch (SVB) of the Custom House, Chennai and an order bearing No. 9458/2009 dated 31.7.2009 was passed accepting the declared value as representing the transaction value. The said order was valid till 30.6.2012. The said order was also accepted by the Commissioner of Customs and thus had attained finality.

3.2 Subsequently, the appellant submitted their request for renewal of the SVB order for the period from 30.6.2012 onwards. In the renewal proceedings, the lower adjudicating authority passed Order-in-Original No. 20346/2013 dated 25.2.2013, wherein he rejected the declared values and directed

a) Addition of technical support and management fee of Rs.11,35,07,299/- paid for the Financial Year 2009 – 10 and Rs.8,83,97,147/- for the Financial Year 2010 – 11 to the value of goods imported during the said years.

b) Loading of declared value @1.6% for imports made upto 19.2.2012 and 2% for imports made since 20.2.2012 till the payment of running royalty and the same was upheld by the Commissioner of Customs (Appeals).

3.3 On the only ground that the manner of computation of royalty was changed from a net sales value basis to a gross sales value basis, the adjudicating authority ordered addition of (a) technical support and management fees paid for the years 2009 – 10 and 2010 – 11 to the value of goods during the said period and (b) loading of invoice value by 1.6% or 2% as the case may be, for the period from 1.4.2011 onwards corresponding to the running royalty payable by the appellant. There is no finding as to whether the payments made on account of Technical Support and Management Fee / royalty met the requires of Rule 10(1)(c) of the Customs Valuation Rules, 2007.

3.4 Ld. Commissioner of Customs (Appeals) did not consider the submission that the sums paid under the MCA were for various types of services such as advice on preparation of budget, forecast, capital expenditure, supply chain management service and global human resources service. For these services, the service fee payable was US$ 450 per man day. These services were not related to the imported goods nor were these payments a condition of sale of the imported goods. There was no finding at all for taking a position contrary to the stand taken by the lower adjudicating authority for the period upto 30.6.2020 which had attained finality. There were no changes in the material facts. The additions confirmed now extended to the imports made during the years 2009 – 10 and 2010 – 11 which is clearly not proper.

3.5 Rule 10(1)(c) of the Customs Valuation Rules, 2007 could be invoked to arrive at the transaction value only on fulfillment of the following essential conditions:-

(i) The royalty / license fee must be related to the imported goods

(ii) It must be required to be paid as a condition of sale of the imported goods and

(iii) It is not already included in the price paid or payable for the imported goods.

3.6 The appellant submits that they were not required to pay royalty or license fee on the imported goods. Nor was there any condition that the appellant was required to import from the suppliers only. The royalty was for the use of the IPR and Technical Information for manufacture of the automotive seating systems in India. The royalty @1.6% or 2% was contingent on the sale of automotive seats manufactured in India. If the imported parts and components are used for the manufacture of automotive seats and the seats could not be sold for any reason then royalty was not payable. Therefore, the said payment is not related to the goods imported by the appellant but to the final product manufactured by the appellant in India. It is submitted that such payments are not covered by Rule 10(1)(c) of Customs Valuation Rules, 2007. In this regard, ld. counsel relied on the following cases:-

(a) Commissioner of Customs Vs. Ferodo India Pvt. Ltd. reported in 2008 (224) ELT 23 (SC)

(b) Taneja Aerospace & Aviation Ltd. Vs. Commissioner of Customs reported in 2008 (228) ELT 159

(c) Panalfa Dongwon India Ltd.v s. Commissioner of Customs reported in 2003 (155) ELT 287 (LB)

3.7 The only ground cited by the Commissioner (Appeals) is that the change in the manner of computing the royalty from a net sale value basis to a gross sales value basis including the landed value of imported components. It is submitted that in the case of Commissioner of Customs, Mumbai Vs. BASF Strenics Pvt. Ltd. – 2006 (195) ELT 206, the Tribunal has held that just because a particular formula has been designed to calculate the royalty amount which also included the raw material cost, it cannot be said that the royalty payment is related to the imported goods. The Tribunal's decision was also approved by the Hon'ble Supreme Court in the case of Commissioner of Customs Vs. Ferodo India Pvt. Ltd. as reported in 2008 (224) ELT 23 (SC). Therefore, mere change in the formula for calculating royalty from net sales value of the product to gross sales value of the product cannot be a justification for addition of royalty and management consultancy fees, when the ingredients for invoking Rule 10(1)(c) are clearly absent.

4. On behalf of the department, ld. AR supported the findings in the impugned order.

5. The issue is whether royalty charges and the service fee stipulated in the management and consultancy agreement can be added to the declared value. For better appreciation, the provision of law as contained under Rule 10(1)(c) of the Customs Valuation (Determination of Price of Imported Goods) Rules, 2007 is noticed as under:-

> "10(1)(c) Royalties and licence fees related to the imported goods that the buyer is required to pay, directly or indirectly, as a condition of the sale of the goods being

> valued, to the extent that such royalties and fees are not included in the price actually paid or payable”

A fleeting look into the respective agreements will bring out the facts for analysis of the issues. The royalty charges have been added to the declared value on the basis of the agreement entered into between the parties. The technical license and assistance agreement by which the royalty charges have been loaded upon in para 2, 4 and 5 reads as under:-

> *“2. Grant of License*
>
> *Subject to the terms and conditions hereinafter set forth, and the licensee duly and fully complying the same, the Licensor hereby grants to the Licensee a non-transferable, non-exclusive right and license to use the Intellectual Property Rights and the Technical Information to manufacture and supply the product to the customer for the lifetime of the vehicle model RBI program. Except stated otherwise in this agreement, the licensee may not sub-license its right under this agreement to any third party without the prior written consent of the Licensor, The grant of license under this section shall <u>be limited to the supply of the product to the customer</u>.*
>
> *4. Technical Assistance*
>
> *4.1 The licensor agrees, <u>upon request of the licensee to sell to the licensee</u> such machinery, tools, and equipment, including but not by way of limitation, jigs, fitting tools, tool gauges, patterns, dies, appliances and other necessary items for the manufacture / assembly of the product at the prices, terms and conditions to be mutually agreed upon by the parties, separately.*
>
> *5. Payments*
>
> *5.1 In consideration of the rights and information as provided in sections 2 and 3 hereof, and in addition to the service fee set forth in section 4 above, the licensee shall pay to the licensor <u>a running royalty of 1.6 percent on the gross sales of the product</u> as long as this agreement is in force. Any regulatory approval in this regard, if required in the Republic of India, shall be obtained by the licensee at its own costs and responsibility”.*

6. The final product sold by the appellant as per the agreement is automotive seating system for vehicles. It can be seen from the conditions of the agreement as reproduced above that there is no compulsion for the appellant to purchase goods / import goods from the licensor. In para 4.1, it is made very much clear that the goods are to be supplied only on request of the appellant. Thus, the payment of royalty is not a condition for importation of goods at all. In fact, the royalty is payable on the gross value of the products sold by the appellant to the customer and is not related to the goods imported by the appellant.

7. The relevant portion of the Management Consultancy Agreement by which the other charges have been loaded by the department reads as under:-

> *"1. Services*
>
> *(a) Subject to the terms and conditions of this Agreement, Dymos shall provide such management consultancy services as fully described in Schedule A (hereinafter the services) to DLSI.*
>
> *(b) The services shall be provided or performed either in DLSI' facilities in the Republic of India or in Dymos' facilitiesi n Korea.*
>
> *(c) DLSI hereby warrants and undertakes that it shall perform its obligations under this agreement and use the services of Dymos in compliance of all applicable laws and legal requirements to which DLSI is subjected to.*
>
> *(d) DLSI hereby fully confirms, understands and acknowledges that while the services would be provided by Dymos in a commercially prudent manner, Dymos does not in any manner warrant or guarantee any effectiveness or suitability to a purpose of such services or any other warranty of whatsoever nature, whether express or implied. Therefore, DLSI shall be using the services solely at its own risks and discretion.*
>
> *2. Payments*
>
> *2.1 Service Fees*

Schedule A - Scope of Service

Dymos will provide the following consultancy and / or advisory services for the operation of DLSI:

1. *Advice concerning the preparation of budgets, forecasts, capital expenditures, financing and long range strategic planning assistance*

2. *Product pricing and costs control and evaluation service*

3. *Customs development service*

4. *Global sourcing service*

5. *Supply chain management service*

6. *Global human resource service and*

7. *Such other services as may from time to time reasonably be requested by DLSI.*

Schedule B – Service Fees

From the date of execution of this Agreement to December 28, 2010, DLSI shall pay Dymos a fee to be calculated at the rate of four hundred fifty US dollars (US$ 45) per man day (including the time required for the service personnel's travel from the origin of the service personnel to DLSI' facilities if travel is necessary)"

8. It can be seen from the above agreement that the charges are paid for the various services rendered and not related to the goods imported.

9. The issue under analysis in this appeal has been considered in various decisions by the Tribunal as well as the Hon'ble Supreme Court. In Commissioner of Customs, Mumbai Vs. BASF Strenics Pvt. Ltd. – 2006 (195) ELT 206, the Tribunal observed as under:-

"9. As regards application of Rule 9(1)(c), we note that only such royalty, payment of which is related to the imported goods and is made as a condition of sale of such goods can be added to the declared price. In the instant case, the payment of royalty is not related to imports of Ethyl Benzene and Styrene Monomer. It appears, the respondents do not have any obligation to import these goods only from their collaborators abroad. It has been noted by the lower authorities that they have in fact imported these goods from non-related suppliers at comparable prices. As such, it cannot be said that the royalties

have been paid as a condition of sale of the imported goods. On the other hand, the agreement between the collaborators abroad and the respondents requires payment of royalty on finished goods manufactured and sold in India. The amount of royalty specified under the agreement relates to sale price of the goods less certain deductions. The applicant Commissioner himself has stated in the grounds of appeal that in effect the royalties are being paid on manufacturing cost plus profit plus the value of raw materials. Just because a particular formula has been designed to calculate the royalty amount which also includes the raw material cost, it cannot be said that the royalty payment is related to the imported goods. In fact, the royalty is payable on the "Net Selling Price" of all "Agreement Products" under the agreement and such products have been defined to mean "polystyrene polymers manufactured in whole or in part according to existing technology or improvement." Such payment of royalty is not therefore restricted to polystyrene polymers manufactured using impugned goods imported from the related suppliers only. We find that the impugned agreement provides for payment of running royalty under the know-how agreement and relates to goods manufactured and sold indigenously. Such payment of royalty to BASF, Germany is for using BASF technology and has also been approved by the R.B.I. In view of the foregoing, we are of the view that the amount of royalty in question cannot be added to the declared value under the said sub-rule (c) either."

10. The Hon'ble Supreme Court upheld the order passed by the Tribunal as reported in 2008 (225) ELT A130 (SC) observing that only when royalty is paid as a condition on sale of imported goods such charges can be loaded to the assessable value for payment of duty.

11. From the above discussions, after appreciating the facts and following the precedence cited above, we are of the considered opinion that the impugned order cannot sustain and the same is set aside. The appeal filed by the appellant is allowed with consequential relief, if any.

(Operative portion of the order was pronounced in open court)

(**SULEKHA BEEVI C.S.**)
Member (Judicial)

(**P. ANJANI KUMAR**)
Member (Technical)

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