

**IN THE CUSTOMS, EXCISE & SERVICE TAX
APPELLATE TRIBUNAL
WEST ZONAL BENCH AT MUMBAI
COURT No. I**

APPEAL No. C/86332/2016

(Arising out of Order-in-Appeal No. MUM-CUSTM-SMP-287/2015-16 dated 8.3.2016 passed by Commissioner of Customs (Appeals), Mumbai-I)

Aquatech Systems (Asia) Pvt. Ltd.

Appellant

Vs.

Commissioner of Customs (Import), Mumbai

Respondent

Appearance:

Shri C.M. Sharma, Consultant, for appellant

Shri R. Kumar, Assistant Commissioner (AR), for respondent

CORAM:

Hon'ble Mr. Ajay Sharma, Member (Judicial)

Hon'ble Mr. Sanjiv Srivastava, Member (Technical)

Date of Hearing: 22.10.2018

Date of Decision: 18.01.2019

ORDER No. **A/85140/2019**

Per: Sanjiv Srivastava

The appeal is directed against the order in appeal No MUM-CUSTM-SMP-287/2015-16 dated 08.03.2016 of Commissioner of Customs (Appeal) Mumbai 1. By the said order Commissioner (Appeal) has upheld the order of Deputy Commissioner of Customs GATT Valuation Cell Mumbai holding as follows:

“a. The importer and the supplier are related in terms of Rule 2(2) of Customs Valuation (Determination of Value of Imported Goods) Rules, 1988/ 2007.

b. I order to enhance the declared invoice value by 10% under Rule 7A of the Customs Valuation Rules, 1988 with an addition mentioned in Table A of para 6.5, year wise for goods imported from the related suppliers for the imports under Rule 9(1)(c) of the Customs Valuation (Determination of Value of Imported Goods) Rules, 1988 up to 09.10.2007 by assessing officer after usual check, scrutiny and verification of the declared value. However, if contemporary imports at higher prices are noticed or there exists reasons other than the influence of relationships to doubt the value assessing group may evaluate the value of the imported goods under appropriate provision of the said rules.

c. I order to enhance the declared invoice value by 10% under Rule 8 of the Customs Valuation Rules, 2007 with an addition mentioned in Table A of para 6.5, year wise for goods imported from the related suppliers for the imports under Rule 10(1)(c) of the Customs Valuation (Determination of Value of Imported Goods) Rules, 1988 from 10.10.2007 by assessing officer after usual check, scrutiny and verification of the declared value. However, if contemporary imports at higher prices are noticed or there exists reasons other than the influence of relationships to doubt the value assessing group may evaluate the value of the imported goods under appropriate provision of the said rules.

d. All the assessments, which have been made final during the period mentioned in Table A para 6.5 shall be taken up in terms of para 7 and suitable demands may be issued in terms of Section 28(1) of the Customs Act, 1962 upto April 2011 and thereafter under Section 28(4)

of the Customs Act, 1962 or any other action under Customs Act, 1962 or any other Law for the time being in force.

e. All pending provisional assessment may be finalized in terms of para 6 and 6.5 of the Order in Review.

f. The above decisions has been taken on the basis of importer's statement, information, affidavit and declaration made in various written submissions made to the department.

g. The order does not take into account any suppression or mis declaration affecting the invoice value, which shall be dealt with approximately under the law and procedure as and when noticed.

h. The decision will remain in force till present method of invoicing remains unchanged. Any change affecting the invoice value materially, be informed to this branch suo motto by the importer without delay.

i. The decision shall be reviewed as and when information additional or contrary to whatever is furnished brought to the notice of this branch.

j. The decision is subject to occasional review/ final review after a period of three years or earlier as the case may be.

k. On expiry of three years period, if no renewal is done this order will stand expired and assessing groups may resort to provisional assessment with RD equivalent to 5% in addition to the loading in terms of para 6 above of assessable value."

2.1 Appellants have been importing goods from their principals M/s Aquatech International Corporation USA and the case of their imports was registered with the special valuation branch (SVB) on 29.03.2006.

Appellants applied for periodical review of SVB order dated 29.03.2006 along with the relevant affidavits and declarations. They submitted that there was no change in the terms and conditions of agreement/ invoicing pattern etc since the time when order dated 29.03.2006 was passed, so their relation was not influencing the transaction value of the imported goods.

2.2 Appellants have vide their letter dated 25.07.2012 submitted royalty details and royalty agreement dated 1.11.2014. After scrutiny of the said royalty agreement and after allowing the personal hearing to the appellants, Deputy Commissioner GATT Valuation Cell passed the order referred in para 1 supra.

2.3 Aggrieved by the order of Deputy Commissioner appellants filed appeal before Commissioner (Appeal). Commissioner (Appeal) initially dismissed the appeal filed by the appellant on ground of limitation as the appeal was filed 26 days beyond the prescribed period for filing the appeal. Against this dismissal appellants filed the appeal before tribunal which was allowed by order No A/695/15/CB dated 11.03.2015 and matter remanded back to Commissioner (Appeal) for decision on merits. Commissioner (Appeal) has in remand proceedings pass this order which is subject matter of the present appeal.

3.1 Appellants have in their appeal challenged the order of Commissioner (Appeal) on various grounds detailed below:

- a) They are not manufacturer of the goods but are engaged in providing consulting engineer/ technology based erection of water treatment plants. The shipments are based on procurement invoices with addition of handling charges. The royalty is not related to import of goods and hence cannot be added to invoice value.
- b) Order for addition to extent of 15% to 25% to the invoice value has been made without disclosing any quantifiable basis for the same.
- c) Appellants have not suppressed any facts from the department at any time.
- d) Despite the fact that related party was charging 10% handling charge over the procurement price from the un-related third party yet loading on the invoice value has been ordered.
- e) The related party i.e their principals in U S A themselves are not the manufacturer of imported goods but they source them from third party. Hence the royalty cannot be related to the impugned goods supplied.
- f) In case of all the imports made through the related person, the value is based on the procurement

price (procurement invoice issued by third party also enclosed to support) plus 10% towards handling charges.

- g) In pre-defined territories as Licensee the related party is the right holder for HERO Technology and in turn royalty is paid by the appellants on project value. The royalty paid is also subjected to Service Tax.
- h) The third party suppliers are not in control of their principals in USA.
- i) The royalty payment is in respect of the Projects executed by them and is linked to the Project Value, wherein the parts are procured and sourced from third party. These procurements from third party cannot be subject matter for the royalty payments.
- j) Thus addition of 15% to 25% to the procurement price is without any basis and is totally arbitrary.
- k) Commissioner has grossly erred in holding that appellants and the supplier are related parties in terms of Rule 2(2) of CVR 1988/ 2007. Further order of Commissioner (Appeal) sustaining the order for making further additions is not justified.
- l) Rule 9(1)(c) of 1988 rules and rule 10(1) (c) valuation rules 2008, allow addition of the "royalty

related to the import goods" which are paid as a condition of sale of the goods imported.

m) In the present case royalty is being paid only on Hero Technology Projects to the related person and it is not as a condition of sale of the imported goods, even when, after their imports, the import goods are disposed of. Provisions of Rule 9(1) (c) of Valuation Rules 1988/ Rule 10 (1) (c) of the Valuation Rules, 2007 are not attracted.

n) Royalty payments are related only to High Efficiency Reverse Osmosis (HERO) technology based projects and is not related to Zero Liquid Discharge (ZLD) Technology or Reverse Osmosis (RO) technology based products, hence addition of royalty charges to the goods imported for executing the projects of later two technologies cannot be justified.

o) Project values on which royalty is paid has no bearing on the import goods and source/ supplier of goods.

p) Royalty herein the present case is related to domestically produced goods and hence provisions of Rule 9(1) (c) of Valuation Rules 1988/ Rule 10 (1) (c) of the Valuation Rules, 2007 are not attracted.

- q) There is no quantifiable basis for rejecting the 10% as margin of handling charges and this is not profit on the prices procured by them from other vendors/ suppliers.
- r) The order is contrary to the interpretative notes to Rule 7A and 9(1) (c) of Valuation Rules , 1988 and Rule 8 and 10(1) (c) of the Valuation Rules, 2007, hence cannot be sustained.

4.1 Have heard Shri C M Sharma Consultant on behalf of Appellants and Shri R Kumar, Assistant Commissioner (Authorized Representative) on behalf of revenue.

4.2 Arguing on the behalf of Appellants learned Consultant submitted:

- i. That it is now settled law that royalty charges can be added to the value of imported goods if it can be show that royalty has been paid as a condition of sale of the said imported goods.
- ii. In the present case royalty is not paid as condition of sale of the said goods, procured by them through the related person. In fact their principals in USA also are not the manufacturers of the imported goods but procure the same from third party. These goods are then supplied to them after addition of 10% towards margin of handling charges on the procurement prices.

- iii. No Quantifiable data has been produced to reject the addition of 10% towards the margin of handling charges, and proposing addition of 10% to the import value in terms of Rule 7A of Valuation Rules, 1988 and Rule 8 of the Valuation Rules, 2007. Thus addition of 10% to the import value in terms of Rule 7A of Valuation Rules, 1988 and Rule 8 of the Valuation Rules, 2007 is totally arbitrary and cannot be sustained.
- iv. Similarly addition of royalty charges to import value without establishing that these royalty charges were related to imported goods and were paid as condition of the sale of said imported goods is contrary to express wordings of Rule 9(1) (c) of Valuation Rules 1988/ Rule 10 (1) (c) of the Valuation Rules, 2007. Hence the order proposing additions of the said charges cannot be sustained.
- v. He relied upon the various authorities as follows in his support-
 - a. Lord India Chemical Products P Ltd [2015 (330) ELT 802 (T-Mum)]
 - b. BASF India Pvt Ltd [2015 (314) ELT 462 (T-MUM)]
 - c. Bridgestone India Pvt Ltd. [2013 (292) ELT 403 (T-Mum)]

- d. Tata Yutaka Autocomp Ltd [2013 (294) ELT 467 (T-Mum)]
- e. Fredo India Pvt Ltd [2008 (224) ELT 23 (SC)]
- vi. Thus he prayed that the appeal be allowed and the order in appeal be set aside.

4.3 Arguing for the revenue learned Authorized Representative submitted-

- i. There is no dispute about the wordings employed in rule 9(1) (c) of Valuation Rules , 1988 and 10(1) (c) of the Valuation Rules, 2007, and the royalty charges need to be added only if they are paid as a condition of sale of the imported goods.
- ii. Tribunal has in case of Mahendra Suiting Ltd [2008 (226) ELT 747 (T-Mum)] held that condition of sale can be an implied one the contract for payment of royalty/ sale of goods need not expressly provide for the same. The projects sought to be implemented could not have been implemented without the technical knowhow for which the royalty charges were being paid. Since the goods have been imported for the implementation of the said project, there is an implied condition for sale of the said goods, Thus addition of royalty charges to the value of imported goods is justifiable and is in accordance with the

provisions of rule 9(1) (c) of Valuation Rules, 1988 and 10(1) (c) of the Valuation Rules, 2007.

- iii. He also submits the issue in respect of addition of royalty charges to the value of imported goods is well settled by the decisions of the Apex Court in case of *Feredo India Pvt Ltd* [2008 (224) ELT 23 (SC)] and *Matsushita Television & Audio (I) Ltd* [2007 (211) ELT 200 (SC)]
- iv. After analyzing the Royalty agreement in para 7 of his order Commissioner (Appeal) has concluded in para 8 that *“post import expenditures shall not be included for the purpose of royalty. Therefore the royalty was paid or would be payable in future by the appellants on the imported goods only and that, not on the other expenses incurred after import. Further it has been rightly observed by the original authority under para 6.4 of the order dated 14.01.2013 that the imported goods were used in the projects using HERO technology, even those goods which are required for the projects, were/ are procured by the supplier for the appellant and supplied to the appellant after adding their 10% margin, which constitutes as a condition of sale”*.
- v. Thus the order of Commissioner in respect of addition of royalty charges to the import value is in accordance with the rule 9(1) (c) of Valuation

Rules, 1988 and 10(1) (c) of the Valuation Rules, 2007, and the decisions rendered by various authority on the subject.

vi. Accordingly he prayed for dismissing the appeal.

5.1 We have considered the submissions made in the appeal and during the argument of appeal. Learned adjudicating authority has in his order dated 14.01.2013, ordered for enhancement of invoice value by 10% under Rule 7A of Valuation Rules 1988/ Rule 8 of Valuation Rules, 2007 and also for addition of royalty charges to value of imported goods in terms of Rule 9(1) (c) of Valuation Rules, 1988 and 10(1) (c) of the Valuation Rules, 2007. Appellants have in their appeal challenged both the additions made.

5.2 For addition made under Rule 7A of Valuation Rules 1988/ Rule 8 of Valuation Rules 2007, adjudicating authority has analyzed the data in respect of the import as tabulated below in table 1-

Description of Item	Procurement		Supplier	
	Invoice No	Price \$	Invoice No	Price \$
NPS 4 A81 Special Tagging/ Field Q Size Q 200DVC6030 RTY PROCESS Level 3	8114102 dtd 15.02.12	4896	ASA-PO 32195 dated 21.02.12	5386
Fisher 6 Inch A81 Butterfly Valve with Field Q Size Q350 Actuator and Type DVC6030 Positioner, steel body Tag-GUK-FCV-3002-028		5890		6476
6" 316 stainless	No	428	ASA-PO 34795-	5471

Steel 150# "Y" Stainers	194193-195 dtd 27.03.12		Y-Stainers-3-26-12 dtd 26.03.12 ASA-PO 347	
4" 316 stainless Steel 150# "Y" Stainers		340		373
LL0001 Spares MB Hela Flow Laterals PVC	1074/10/295 dtd 24.12.10	2425	803129 dtd 28.12.10	2668
LL0002 Spares MB HastC Wedge Wire Flanges		3250		3575
LL0003 Spares MB Middle Collector Distributor Freight		3821		4204
Flow Relief Valve	GP 52856 dtd 16.02.10	27540	ASA Site AE 1014-10348-0910-2-16-10 dtd 16.02.10	30600

5.3 After recording the said data Adjudicating authority has given findings as follows:

"On perusal of the tables, it is seen that the goods were first imported/procured by M/s. Aquatech International Corporation, USA either from their local vendors in the different cities of USA or imported from other countries on CIF basis and after that the said products were supplied to M/s. Aquatech Systems (Asia) Pvt. Ltd. on CIF basis in India. On comparison of the prices of the in terms of rule 3(3)(b)(iii) ibid in column 4 & 6 of the Table I find that the supplier has taken nearly 10% margin of profit on the prices procured by them from other vendors. In a normal trade practice, if the goods are being exported to India by the suppliers, there are some addition like marketing, selling expenses, administrative and other general expenses, tax liability, depreciation of the factory investments, loading, unloading charges, handling charges, internal freight charges, insurance profit etc in determining the prices for the purpose of export. This all addition constitutes from 15% to 25% in addition to the procured prices. However, only 10% has been added by the supplier for exportation of the goods to the Indian importer. Accordingly, the invoice value may be loaded to the tune of 10% in terms of Rule 8 of Customs Valuation Rules, 2007 read

with section 14 of the Customs Act, 1962 (as amended time to time)."

5.4 Though these findings and addition were challenged by the appellant in their appeal before the Commissioner (Appeal), Commissioner (Appeal) has not recorded any finding in his order in this respect. Hence matter for consideration of additions as ordered by the adjudicating authority under Rule 7A of Valuation Rules 1988/ Rule 8 of Valuation Rules 2007 needs to be remanded back to the Commissioner (Appeal) for consideration of the issue.

6.1 Rule 9(1) (c) of the Customs Valuation Rules 1988 has been analyzed by the Hon'ble Apex Court in the case of Ferodo India Pvt Ltd [2008 (224) ELT 23 (SC)]. The relevant para of the Apex Court decision are reproduced below:

"Analysis of Rule 9(1)(c)

15. *Rule 9(1)(c) extends the quantum of levy under Rule 4. Rule 9(4) mandates that there can be addition to the transaction value except as provided in Rule 9(1) and (2). Hence, addition for cost can only be made in situations coming under Rule 9(1) and (2). Rule 9(1) and (2) is based on the principle of attribution. Under Customs law, valuation is done on pricing whereas in the case of transfer pricing under Income-tax Act, 1961, valuation is profit based. The principle of attribution of certain costs (including royalty and licence fee payments) to the price of the imported goods is provided for in Rule 9 under situations mentioned in Rule 9(1) and (2). In transfer pricing, the arm's length price is inferred from various methods to avoid profit-shift from one jurisdiction to another*

and it is here that principle of allocation of profits comes in (i.e. in the case of transfer pricing).

16. *Under Rule 9(1)(c), the cost of technical know-how and payment of royalty is includible in the price of the imported goods if the said payment constitutes a condition pre-requisite for the supply of the imported goods by the foreign supplier. If such a condition exists then the payment made towards technical know-how and royalties has to be included in the price of the imported goods. On the other hand, if such payment has no nexus with the wording of the imported goods then such payment was not includible in the price of the imported goods.*

17. *In the case of Essar Gujarat Ltd. (supra) the condition pre-requisite, referred to above, had direct nexus with the functioning of the imported plant and, therefore, it had to be loaded to the price thereof.*

18. *Royalties and licence fees related to the imported goods is the cost which is incurred by the buyer in addition to the price which the buyer has to pay as consideration for the purchase of the imported goods. In other words, in addition to the price for the imported goods the buyer incurs costs on account of royalty and licence fee which the buyer pays to the foreign supplier for using information, patent, trade mark and know-how in the manufacture of the licensed product in India. Therefore, there are two concepts which operate simultaneously, namely, price for the imported goods and the royalties/licence fees which are also paid to the foreign supplier. Rule 9(1)(c) stipulates that payments made towards technical know-how must be a condition pre-requisite for the supply of imported goods by the foreign supplier and if such condition exists then such royalties and fees have to be included in the price of the imported goods. Under Rule 9(1)(c) the cost of technical know-how is included if the same is to be paid, directly or indirectly, as a condition of the sale of imported goods. At this stage, we would like to emphasis the word indirectly in Rule 9(1)(c). As stated above, the*

buyer/importer makes payment of the price of the imported goods. He also incurs the cost of technical know-how. Therefore, the Department in every case is not only required to look at TAA, it is also required to look at the pricing arrangement/agreement between the buyer and his foreign collaborator. For example if on examination of the pricing arrangement in juxtaposition with the TAA, the Department finds that the importer/buyer has misled the Department by adjusting the price of the imported item in guise of increased royalty/licence fees then the adjudicating authority would be right in including the cost of royalty/licence fees payment in the price of the imported goods. In such cases the principle of attribution of royalty/licence fees to the price of imported goods would apply. This is because every importer/buyer is obliged to pay not only the price for the imported goods but he also incurs the cost of technical know-how which is paid to the foreign supplier. Therefore, such adjustments would certainly attract Rule 9(l)(c)."

6.2 Hon'ble Supreme Court has in case of Matsushita Television & Audio (I) Ltd [2007 (211) ELT 200 9SC] held as follows:

"6. *On reading the above agreement, the following features emerge. Under Clause 1.03 the term "Net-factory sale price" has been defined to mean the sale price billed by the appellants for its products to its customers in normal arm's length transaction exclusive of taxes, freight and insurance, but including the cost of the bought-out components and the cost of the imported components. Under Clause 1.04 the term "Technical Know-how" was defined to mean technical information required for the manufacture of colour T.V. as specified in Clause 3.01. The technical know-how which was agreed to be furnished to the appellants was to consist of quality control standard and specification of the components to be used in the manufacture of T.V. sets. Further, under Clause 2.01 it was agreed that MEI shall render to the*

appellants the technical assistance regarding the manufacture of the T.V. sets in the manner provided in the said clause. Under the said Clause 2.02(C), all costs, charges and expenses, incurred by the appellants for technical assistance, was to be paid by the appellants in U.S. Dollars. Further, under Clause 4.01, MEI agreed to grant to the appellants a licence to use the technical assistance and the technical know-how for the manufacture of the colour T.V. at the appellants' factory in India and also for sale of such products throughout India. Under Clause 6.01, in consideration of the technical assistance to be rendered by MEI and in consideration of the licence to be granted by MEI to the appellants it was agreed that the appellants shall pay to MEI the royalty at the rate of 3% on the net ex-factory sale price of the colour T.V. manufactured and sold. Further, it was agreed that in addition to the technical assistance, MEI would assist the appellants in the manufacturing of the colour T.V. by selling the components to the appellants. Under the Agreement, the parties further agreed that if the appellant desired to make use of bought-out components it can do so provided the said components are forwarded to MEI for inspection and if MEI approves the quality and the specifications of such bought-out components then alone the appellant would be free to use such components in the manufacture of colour T.V.

7. *The question which arises for consideration in this civil appeal is : whether royalty payment was connected with the imported components. Under Rule 9(1)(c) of the Valuation Rules, 1988, only such royalty which is relatable to the imported goods and which is a condition of sale of such goods alone could be added to the declared price. However, in the present case, payment of continuing royalty was payable at the rate of 3% of the net ex-factory sale price of the colour T.V. exclusive of taxes, freight and insurance but including the cost of imported components. In other words, the royalty payment was to be computed not only on the domestic element of the net sale price of the colour T.V. but also on the cost of imported components. A bare reading of the agreement shows that*

payment under the said agreement related not only to the production of the goods in India but also to imports. In some of the decisions cited on behalf of the assessee, we find that the net ex-factory sale price of the finished products expressly excluded the cost of imported components. On the other hand, in the present case, the cost of imported components was expressly included in the net ex-factory sale price of the colour T.V. Further, when payment to MEI was at the rate of 3% of the sales turn over of the final product, including cost of imported component, it became a condition of sale of the finished goods. Hence, in this case both the conditions of Rule 9(1)(c) of the Valuation Rules, 1988, are satisfied.”

6.3 Thus the law laid down by the Hon'ble Apex Court in the above two decisions, is that only that royalty element which is related to the imported goods and is a condition for sale of the goods is includible in value of the imported goods for the purpose of Rule 9(1)(c) of Valuation Rules 1988. By reading of the royalty agreement in the case of Matsushita Televisions, specifically the definition of net sale price in the said agreement “*“Net-factory sale price” has been defined to mean the sale price billed by the appellants for its products to its customers in normal arm's length transaction exclusive of taxes, freight and insurance, but including the cost of the bought-out components and the cost of the imported components.”*, Hon'ble Apex Court concluded that *“the cost of imported components was expressly included in the net ex-factory sale price of the colour T.V. Further, when payment to MEI was at the rate*

of 3% of the sales turn over of the final product, including cost of imported component, it became a condition of sale of the finished goods.”

6.4 Examining the terms of Royalty Agreement in the present case wherein it has been stipulated *“in consideration for use of HERO Technology, ASA shall pay to AIC, Royalty @ 5% of the project value, subject to reduction towards freight outwards, commission, spare parts cost and field services, and also subject to applicable taxes in India. The project value shall be net amount, excluding any statutory levies, recoverable from the client. In case of the projects under Build, Own, Operate, and Transfer contracts, (hereinafter referred to as BOOT arrangement) the project value shall be the net amount of the total capital cost incurred on the BOOT Plant excluding any statutory levies and amounts applicable for BOOT arrangement”*. Appellants have given the explanation of the said clause in the Royalty agreement, in following manner:

“Royalty Calculation Basis

Royalty is payable @5% of the project value for use of HERO™ process license, subject to reduction towards freight outwards, commission, spare part costs and field services and also subject to applicable taxes in India. The project value shall be net amount excluding any statutory levies, recoverable, from the client. Following is the basis of calculation of Royalty for TCI Sanmar Project

Description	Amount (INR)
Contract Value	22,4250847.00
LESS	
Freight Out	4,00,000.00
Commission & Royalty Prov	56,02,500.00
Spare Parts	
Field Service Cost	
Total Cost	21,82,48,347.00
Royalty @ 5%	1,09,12,417.00”

6.5 The above clearly shows that value of the imported goods is included in “project value” and royalty has been paid on the project value determined inclusive of the value of imported goods. Thus in terms of the law laid down by the Apex Court in case of Matsushita Televisions, the conditions for addition of royalty charges as laid down in Rule 9 (1)(c) of the Valuation Rules, 1988 are satisfied in the present case. In case of Ferodo India Pvt Ltd, Hon’ble Apex Court has clarified about the decision in case of Essar Gujarat Ltd [1996 (88) ELT 609 (SC)] & Matsushita Televisions stating

“**22.** In the case of Essar Gujarat Ltd. (supra), the buyer had entered into a contract with TIL for purchase of Direct Reduction Iron Plant (“the plant”). The entire agreement was for import of the plant. The agreement was subject to two conditions- (a) approval of G.O.I. and (b) obtaining transfer of licence from M/s. Midrex, USA. Without the licence from Midrex, the imported plant was of no use to the buyer. Therefore, it was essential to have the licence from Midrex to operate the plant. Therefore, it was held by this Court that procurement of licence from Midrex was a pre-condition of sale which was specifically recorded in the agreement itself. In view of specific terms and conditions to that effect in the

agreement, this Court held that payments made to Midrex by way of licence fees had to be added to the price paid to TIL for purchase of the plant. There is no such stipulations in the TAA in the present case. Therefore, in our view, the adjudicating authority erred in placing reliance on the judgment of this Court in Essar Gujarat Ltd. (supra).

23. *In the case of Matsushita Television & Audio India Ltd. v. CoC reported in 2007 (211) E.L.T. 200 (S.C.) the question which arose for determination was whether royalty amount was attributable to the price of the imported goods. In that case, the appellant was a joint venture company of MEI, Japan and SIL for obtaining technical assistance and know-how. Under the agreement, the appellants were to pay MEI a royalty @ 3% on net ex-factory sale price of the colour TV receivers manufactured by the appellants for the technical assistance rendered by MEI. The appellants were to pay a lump-sum amount of U.S. \$ 2 lakhs to MEI for transfer of technical know-how. It was the case of the appellant that payment of royalty was not related to imported goods as the said payment was made for supply of technical assistance and not as a condition pre-requisite for the sale of the components.*

24. *One of the questions which arises for determination in this civil appeal is whether reliance could be placed by the Department only on the Consideration Clause in the TAA for arriving at the conclusion that payment for royalty was includible in the price of the important components.*

25. *Rule 4(3)(b) of the CVR, 1988 provides for an opportunity for the importer to demonstrate that the transaction value closely approximates to a “test” value. A number of factors, therefore, have to be taken into consideration in determining whether one value “closely approximates” to another value. These factors include the nature of the imported goods, the nature of the industry itself, the difference in values etc. As stated above, Rule 4(3)(a) and Rule 4(3)(b) of the CVR, 1988 provides for different means of establishing the acceptability*

of a transaction value. In the case of Matsushita Television (supra) the pricing arrangement was not produced before the Department. In our view, the Consideration Clause in such circumstances is of relevance. As stated above, pricing arrangement and TAA are both to be seen by the Department. As stated above, in a given case, if the Consideration Clause indicates that the importer/buyer had adjusted the price of the imported goods in guise of enhanced royalty or if the Department finds that the buyer had misled the Department by such pricing adjustments then the adjudicating authority would be justified in adding the royalty/licence fees payment to the price of the imported goods. Therefore, it cannot be said that the Consideration Clause in TAA is not relevant. Ultimately, the test of close approximation of values require all circumstances to be taken into account. It is keeping in mind the Consideration Clause along with other surrounding circumstances that the Tribunal in the case of Matsushita Television (supra) had taken the view that royalty payment had to be added to the price of the imported goods.”

6.6 Thus in view of the decision of the Apex Court the order of Commissioner (Appeal) upholding addition of royalty charges cannot be faulted with. Adjudicating authority has in his order dealt the issue of Royalty stating-

“6.2 From the contents of the agreement, I find that the royalty is payable to the supplier for enabling the HERO Technology. Both, importer and suppliers are engaged in the water treatment/waste water treatment process. Both are playing a role of contractors and obtaining the trunk projects for water/wastewater treatment with the application of HERO Technology. They are not the manufacturer of the components/spare parts of the equipments. Both the importers and suppliers are procuring the goods/spare parts, components,

equipments for their projects. Hence, if any spare parts, components or any equipments are required for the completion of the projects, they are supposed to procure the materials from different vendors. However, the importers have chosen the suppliers to supply these spare parts/components/equipments to supply the importers. They were in a binding situation to import these goods from the related suppliers. Although they were free to import from the unrelated vendors. Now the question is whether the Royalty, which is being paid or payable as per the Royalty Agreement dated 01.11.2004, is includable to the assessable value of the imported goods or not? I find that there are various judgments viz. M/s. Ferodo India Pvt. Ltd. [2008(224)ELT 23(SC)], M/s. Toyota Kirloskar Motor Pvt. Ltd. [2007(231)ELT 4(SC)] and M/s. Steel Authority of India [2007(210)ELT150(Tri-Bang)] wherein, Hon'ble Supreme Court and CESTAT have held that Technical Know How fees and Royalty is includible in prices of imported goods, if said payments constitutes a condition pre-requisite for supply of imported goods by foreign suppliers. If such payment has no nexus with working of imported goods then such payment was not includible in prices of imported goods. Therefore, it will be relevant to examine whether there is any pre-requisite condition on the importation of goods or not?

6.3 As far as condition of sale is concerned, the terms of the any Agreement may not explicitly refer to the obligation to pay fee/royalty as a condition of sale. Hence, the entire financial circumstances, surrounding the transaction are to be examined so as to see the material aspects of the commercial arrangements between the importer and the foreign supplier regarding the imported goods. In the instant case, the royalty

amount payable on the contract value attributable to the use of HERO Technology in the project subject to reduction of freight outwards, commission, spare parts cost and field services. In consideration of HERO technology, the ASA shall pay to AIC, Royalty @5% of the project value. Any project, which has been granted to the ASA, a contractor, will not be completed either with the imported goods or with the HERO technology, such an obligation should constitute a condition of sale.

6.4 Further, on verification of facts, which has been accepted by the importers at the time of personal hearing on 11.01.2013 that the imported goods are used in the projects using the HERO technology, even those goods, which are required for the projects, were/are procured by the supplier for the importers and supplied to the importers after adding their 10% margin, which constitutes as a condition of sale. In the case of Commissioner of Customs versus Mahendra Suiting Limited [2008 (226) ELT 747] the Tribunal held that the condition for sale can be implied and the contract need not expressly provide for it.

6.5 Further, I find that while calculating the Royalty on the total project value, even the imported spare parts/components/equipment are included, although, in the agreement, the value of the spare parts has to be excluded from the project value, therefore, the royalty needs to be added to the value of imported goods under Rule 10(1)(c) of the Customs Valuation Rules, 2007. Importer vide their letter dated 10.01.2013 has submitted the total Royalty and value of imports for the last 5 years, which are reflected in their annual audited balance sheets, on the basis of which Royalty may be added to the value of imported goods covered under the Royalty Agreements effective from 01.11.2004. Although

they are paying royalty from Nov. 2004, however, the Customs Act, 1962 provides recovery of duty for last 5 years under Section 28(1) upto April 2011 and under Section 28(4) thereafter. Hence, the % of loading on assessable value with respect to total amount of Royalty paid on the imported goods may be determined as per formula as under for the last 5 years:-

$$\text{Loading \% on Assessable Value} = \text{Royalty paid} \times 100$$

(Reference column (4) below)

Value of imported goods

Year	Amount of Royalty paid to the suppliers (in Rs.)	Value of imported goods (in Rs.)	% Loading
(1)	(2)	(3)	(4)
2006-07	NIL	12,33,261 / -	0
2007-08	1,07,64,657 / -	30,09,297 / -	357.71%
2008-09	NIL	23,74,263 / -	0
2009-10	50,92,162 / -	33,91,842 / -	150.13%
2010-11	79,76,380 / -	5,19,680 / -	1534.86%
2011-12	NIL	29,36,713 / -	0

6.7 Appellants have in their appeal and during course of arguments raised various other issues which are listed as follows:

- i. Royalty payment is only in respect of the project based on HERO Technology and not in respect of the projects based on other technologies i.e. ZLD & RO

- ii. Royalty payments have been made also in respect of certain projects executed outside India.
- iii. There is no suppression of facts.

6.8 In para 7 of his order, adjudicating authority has specifically dealt with the issue of suppression in para 7 of his order which reads as follows:

“7. I further find that although the importers have stated vide their letter dated 15.07.2010 that there has been no change in the method of invoicing or pricing and transaction value is at arm's length and price is the sole consideration for the transaction and filed an affidavit affirming themselves regarding this. However, I find that even before passing of earlier order dated 23.03.2006/03.04.2006, there was an agreement viz. “Royalty Agreement” w.e.f. 01.11.2004, which was never brought to the notice to the quasi-judicial authority for consideration, as to whether, the said agreement is going to influence the prices of imported goods or not and because of this reason the prices of the imported goods from their related suppliers were accepted under Rule 4(3) of the Customs Valuation Rules, 1988. Even at the time of filing their application for periodical review vide their letter dated 15.07.2010, they have not stated anything about the Royalty Agreement and submitted various other documents but not the said agreement. Further in their reply no. 21 of the Questionnaire, they have stated that NIL amount is paid and payable for royalty is paid or payable to the supplier of the imported goods. In the order dated 23.03.2006/03.04.2006, even after mentioning, that this order does not take into account any suppression or mis-declaration affecting the invoice value, which shall be dealt with appropriately under the law and procedure as and when detected, the importers have never informed about payment of Royalty and suppressed the vital facts about the execution of Royalty Agreement dated 01.11.2004, which ultimately going to effect

the transaction value of the imported goods. Therefore, I find that this case is rightly covered under the provisions of Section 28(1) of the Customs Act, 1962 upto April 2011 and under Section 28(4) of the Customs Act, 1962, thereafter (as amended time to time) or any other action under Customs Act, 1962 or any other law for the time being in force.”

6.9 On the other issues adjudicating authority has himself held and asked appellants to submit proportional quantum of royalty for each consignment.

Para 6.6 of the order reads as follows:

“6.6 From the above, it is seen that the % loading is dependent upon the quantum of import and quantum of royalty paid to the suppliers as the “project value of the contract”, on which the patented trade mark “HERO” technology is used, may vary year to year basis. Similarly, the quantum of import may vary year to year basis. Hence, to ascertain the quantum of % loading to the assessable value for the live consignments, the Royalty may be loaded proportionately to the assessable value under Rule 10(1)(c) of the Customs Valuation Rules, 2007. The importers should come forward to submit the proportional quantum of Royalty for each consignment, duly certified by independent Chartered Accountant, imported by them from their related supplier voluntarily, so that the assessing Officer can calculate the % of loading in the assessable value at the time of importation.”

6.10 In view of the above discussions we do not find any merits in the submissions of the appellants in relation to addition of royalty charges in the value of imported goods in terms of Rule 9 (1) (c) of Valuation Rules, 1988/ Rule 10(1)(c) of Valuation Rules 2007.

6.11 Appellants have in their appeal and during arguments relied upon various decisions of the Tribunal

holding that Royalty Charges cannot be added to the value of imported goods. We do not dispute the preposition laid down in the said decisions but in terms of the decisions Apex Court as referred above, the issue of addition of Royalty Charges will be dependent on the terms and condition of Royalty agreement. In the decisions referred by the appellants tribunal has after examining the terms of the agreement in those cases concluded that in facts of that case royalty charges could not have been added.

6.12 In the result, appeal is partially allowed by way of remand as indicated in para 5.4 of this order.

(Pronounced in court on 18.01.2019)

(Ajay Sharma)
Member (Judicial)

(Sanjiv Srivastava)
Member (Technical)