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TAX FLASH NEWS

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Supreme Court affirms that activity of advertisement and sales promotion is a post import activity incurred suo-motu by the importer and thus not liable to be included in assessable value of imports

Rule 10(1)(e) of the Customs Valuation (Determination of Value of Imported Goods), 2007 states that in determining the transaction value, 'Importer' should include all other payments made as a condition of sale of the imported goods to the transaction value.

In this regard, Supreme Court[1] has affirmed that the activity of advertisement and sales promotion is a post import activity incurred by the importer on its own account and not for discharge for any obligation of the seller under the terms of sale.

Facts of the case

- 'Importer' is engaged in manufacture of sports goods under its own brand name as well as engaged in import and distribution of sports goods of its 'Seller' located in Singapore under the Seller's brand name.
- 'Distribution Agreement' was entered into between 'Importer' and 'Seller' for import and sale of sports goods throughout the territory of India except three states. The said agreement had clauses which stated that the 'Importer' will use its best endeavors to promote and extend sales of goods within the territory and also stated that 'Importer' will bear all costs of advertisement, marketing and promotions (AMP) for the territory.
- 'Seller' entered into separate sponsorship agreements with Sports Associations and Sports Personalities for promotion of its brand within India. Such agreements were signed by the Manager of the 'Importer' on behalf of 'Seller' / 'Importer'.
- 'Revenue' issued and adjudicated show cause notice on the following grounds :
  - AMP expenses made by the 'Importer' to promote the brand of 'Seller' was a condition of sale and thus liable to be included in the value of imports in terms of Rule 10(1)(e);
  - 'Seller' would not have appointed 'Importer' as a sole distributor had the 'Importer' not agreed to bear such cost;
  - Manager of 'Importer' signed the sponsorship agreements.

Importer's contentions before the Tribunal

- It is not the sole and exclusive agent and there are other agents appointed by the 'Seller' for distribution of its products in India;
- There is nothing in the 'Distribution Agreement' which binds itself to incur any fixed amount or percentage of import value of the goods or the invoice value of goods. The post import cost for publicity is at the discretion of the 'Importer' and the agreement further stipulates that the expenditure made is in consultation of the 'Seller'.
- Manager of the 'Importer' has signed the 'Sponsorship Agreements' because from the combined reading of the 'Distribution Agreement' with 'Sponsorship Agreements' , it is the 'Importer' who is liable to pay the amount or provide goods to such Associations / Sports Personalities. Further, the payments made to Sports Associations and the Sports Personalities are by the 'Importer' and not on behalf of 'Seller';

[1] The Commissioner of Customs Vs M/s Indo Rubber And Plastic Works [2021-VIL-68-SC-CU]

- Rule 10(1)(e) does not apply as there is no pre-condition imposed on the 'Importer' to incur any particular percentage or amount towards sales promotion / advertisement.

Revenue's contentions before the Tribunal

- AMP expenses incurred by 'Importer' on behalf of the 'Seller' is includible in the assessable value of the imported goods, as provided in first proviso to section 14(1) of Customs Act, 1962.

- It further contended that the said proviso prescribes that any amount paid or payable for cost and services, on behalf of the seller, is to be added to the transaction value, to the extent in the manner specified in the Rules made in this behalf. In the instant case, all the ingredients are available for Rule10(1)(e) to apply;

- Sponsorship Agreements are signed by the Manager of the 'Importer'. Sponsorship and promotional expenses are borne by 'Importer' which were supposed to be borne by 'Seller'. Thus, it is established that there is a pre-condition.

Tribunal's decision

'Tribunal' had allowed the appeal in favor of the 'Importer' stating that –

- There is nothing in the agreement that a fixed amount or fixed percentage of invoice value of imported value of imported goods is to be spent by 'Importer' as a condition of sale / import;

- Activity of advertisement and sales promotion is a post import activity by 'Importer' on its own account and not for discharge of any obligation of 'Seller' under terms of sale.

Supreme Court's decision

'Revenue' filed an appeal before the Hon'ble Supreme Court. It refused the admission of the appeal holding that there are no merits in the appeal and thus upheld the decision of the Tribunal.

Our comments

Promotional activities are equally relevant for related party transaction and third-party transaction and it has both customs and transfer pricing dimension. A determination on inclusion of AMP expenses in customs valuation is a fact-based exercise which requires examination of contractual arrangements between the buyer and the seller and testing the substance of AMP activity. It's a welcome judgment, though the issue may continue to be debated and discussed at various judicial and quasi-judicial forums, specially in relation to related party transactions.

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