CUSTOMS, EXCISE AND SERVICE TAX APPELLATE TRIBUNAL
<u>CHENNAI</u>

REGIONAL BENCH – COURT No. I

Customs Appeal No. 40187 of 2016

(Arising out of Order-in-Appeal C.Cus II No. 824/2015 dated 03.09.2015 passed by the Commissioner of Customs (Appeals-II), No. 60, Rajaji Salai, Custom House, Chennai – 600 001)

M/s. CET Power Solutions India Pvt. Ltd. **...Appellant**
No. 2/295, DRR Avenue,
Audco Nagar,
Kattupakkam,
Chennai – 600 056.

Versus

Commissioner of Customs **...Respondent**
Chennai III Commissionerate,
No. 60, Rajaji Salai,
Custom House,
Chennai – 600 001.

<u>APPEARANCE:</u>

For the Appellant : Mr. M. Karthikeyan, Advocate
For the Respondent : Mr. Sanjay Kakkar, Authorised Representative

<u>CORAM:</u>
HON'BLE MR. VASA SESHAGIRI RAO, MEMBER (TECHNICAL)
HON'BLE MR. AJAYAN T.V., MEMBER (JUDICIAL)

<u>FINAL ORDER No. 41033 / 2026</u>

DATE OF HEARING : 12.06.2026
DATE OF DECISION : 22.09.2026

Per Mr. VASA SESHAGIRI RAO

The present appeal has been filed by M/s. CET Power Solutions India Pvt. Ltd. (hereinafter referred to as "the appellant") challenging Order-in-Appeal No. 824/2015 dated 03.09.2015 (hereinafter referred to as "the impugned order") whereby the Commissioner of Customs (Appeals-II), Chennai upheld Order-in-Original No. 38622/2015 dated 10.06.2015 passed by the Deputy Commissioner of Customs, Special Valuation Branch, Chennai, holding that royalty payments made by the appellant to its foreign related supplier were includible in the assessable value of imported goods under the Customs Valuation Rules, 2007.

2. The appellant, a 100% Export Oriented Unit engaged in manufacture of power conversion and inverter systems, imports goods from its related foreign suppliers, namely M/s. CE+T SA, Belgium and M/s. Suzhou CE+T Power Solutions Co. Ltd., China. During Special Valuation Branch investigation, the Department entertained a view that royalty paid by the appellant under agreements with the foreign collaborator was liable to be added to assessable value under the Customs Valuation Rules, 2007. In the first round, Order-in-Original No 24406/2014 dated 14.03.2014 accepted the declared transaction value and held that royalty was not includible; however, on Revenue appeal, the matter was remanded for fresh examination. Pursuant thereto, de novo Order-in-Original dated 10.06.2015 held that royalty was includible in assessable value on the ground that imported components constituted integral raw materials for manufacture of CE+T branded products, which finding came to be affirmed by Order-in-Appeal dated 03.09.2015, against which the present appeal has been filed.

3. The Ld. Advocate Shri M. Karthikeyan appearing for the appellant, submitted that the impugned order proceeds on an erroneous interpretation of Rule 10(1)(c) of the Customs Valuation Rules, ignoring the settled principle that royalty can be added to assessable value only when such payment relates to imported goods and constitutes a condition of sale. It was submitted that the original adjudicating authority had rightly held in the first round that royalty was not includible, but Revenue secured remand without demonstrating any legal infirmity. Learned counsel submitted that under the Term Sheet dated 06.03.2008, Royalty Agreement dated 01.04.2010 and Licence Agreement dated 01.04.2012, the foreign collaborator had granted manufacturing rights, technical know-how, patents, trademarks and engineering support for manufacture of CE+T products in India, while royalty at 2% was payable only on turnover or net selling price of finished products manufactured and sold in India. It was argued that none of the agreements stipulated that import of raw materials or components was conditional upon payment of royalty and the royalty represented consideration for post-import manufacturing rights and commercial exploitation of intellectual property. Learned counsel further submitted that Rule 10(1)(c) requires satisfaction of two cumulative conditions, namely that royalty must relate to imported

goods and payment thereof must constitute a condition of sale, both of which are absent in the present case. The Department, according to the appellant, had merely proceeded on the assumption that since imported components were used in manufacture, royalty automatically became includible, which is contrary to settled law. In support, reliance was placed upon Commissioner of Customs Chennai v BBL Daido Pvt Ltd, Ferodo India Pvt Ltd v Commissioner of Customs Mumbai, Toyota Kirloskar Motor Pvt Ltd v Commissioner of Customs Bangalore and other decisions.

4. *Per contra*, the Ld. Authorized Representative Shri Sanjay Kakkar appearing for the Revenue reiterated the findings of the impugned order and submitted that the appellant and the foreign supplier were admittedly related entities and the entire arrangement involving import of components, manufacture of CE+T branded products and payment of royalty constituted an integrated commercial framework. It was contended that the royalty payments could not be viewed independently since imported components formed the essential basis for manufacture of finished products in respect of which royalty was paid. According to Revenue, although royalty was quantified on net selling price, the finished goods could not have been

manufactured without imported components sourced from the foreign collaborator and therefore the royalty payment had direct nexus with the imported goods. It was further argued that the appellant had failed to establish that imported component cost stood excluded while calculating royalty and once imported goods constituted as integral raw materials for manufacture of branded finished products, the requirement of nexus under Rule 10(1)(c) stood satisfied. Revenue therefore contended that the adjudicating authority had rightly added royalty to assessable value and prayed for upholding the impugned order.

5. We have carefully considered the rival submissions, examined the records placed before us including the Term Sheet dated 06.03.2008, Royalty Agreement dated 01.04.2010, Licence Agreement dated 01.04.2012, the first Order-in-Original dated 14.03.2014, Order-in-Appeal dated 26.08.2014 remanding the matter, de novo Order-in-Original dated 10.06.2015 and the impugned Order-in-Appeal dated 03.09.2015, and have also considered the judicial precedents relied upon by both sides.

6. The short questions which arise for determination in the present appeal are as follows: -

i. Whether royalty paid by the appellant is includible in the assessable value of imported goods under Rule 10 of the Customs Valuation Rules, 2007?

ii. Whether the impugned orders confirming such inclusion are legally sustainable?

7. We now proceed to examine the issues arising for determination in the present appeal sequentially.

Issue No. (i): Whether royalty paid by the appellant is includible in the assessable value of imported goods under Rule 10 of the Customs Valuation Rules, 2007?

8. The principal issue requiring determination in the present appeal is whether royalty payments made by the appellant under the contractual arrangements entered into with its foreign collaborator are liable to be included in the assessable value of imported goods under Rule 10(1)(c) read with Rule 10(1)(e) of the Customs Valuation (Determination of Value of Imported Goods) Rules, 2007. For proper appreciation, the statutory provision itself requires examination. Rule 10(1)(c) provides that royalties and licence fees shall be added to the price actually paid or payable only where such royalties are related to the imported goods and the buyer is required to pay the same, directly or indirectly, as a condition of sale of the imported goods being valued. The statutory scheme therefore makes it

abundantly clear that royalty payments do not automatically become includible merely because they are paid by an importer to their foreign collaborator.

9. A plain reading of Rule 10(1)(c) shows that two cumulative statutory conditions must coexist before any addition can be sustained. First, the royalty payment must be related to the imported goods. Secondly, payment of such royalty must constitute a condition of sale of the imported goods. Unless both these requirements are affirmatively established by the Department, enhancement of assessable value to include Royalty cannot legally be sustained. The burden to establish these statutory ingredients squarely lies upon the Revenue.

10. We also find that Revenue has sought to rely upon Rule 10(1)(e) of the Customs Valuation Rules, 2007, which provides for addition of all other payments actually made or to be made as a condition of sale of the imported goods by the buyer to the seller or to a third party in satisfaction of an obligation of the seller. The Explanation appended to Rule 10 further clarifies that where royalty, licence fee or any other payment for a process, whether patented or otherwise, is includible under clauses (c) and (e), such charges shall be added notwithstanding the fact

that the imported goods may be subjected to such process after importation. In our considered opinion, neither Rule 10(1)(e) nor the Explanation advances the Revenue's case. The Explanation appended to Rule 10 cannot be read as creating an independent charging mechanism or enlarging the substantive scope of clauses (c) and (e); it merely clarifies that once the primary statutory conditions are satisfied, subsequent processing after importation would not exclude inclusion. In the present case, the Department has failed to establish that the royalty paid by the appellant under the contractual agreements was an obligation intrinsically linked to sale of the imported goods. The agreements demonstrate that the payments were made towards technology transfer, intellectual property rights and post-import manufacturing rights and not as consideration flowing from the import transaction itself. Consequently, invocation of Rule 10(1)(e) and its Explanation is equally misconceived.

11. In the present case, the Department proceeds substantially on the assumption that since the appellant imports components from its foreign related supplier and uses such components in manufacture of CE+T branded finished products, royalty paid by the appellant automatically becomes connected with imported goods. Such reasoning, in

our considered opinion, proceeds on an impermissibly broad interpretation of Rule 10 and overlooks the settled distinction between payments connected with importation and payments arising out of post-import manufacture. Customs valuation jurisprudence consistently recognizes that royalty paid for technical know-how, intellectual property rights, trademarks, manufacturing rights and post-import commercial exploitation cannot automatically be loaded into assessed value of imports merely because imported components are used for the manufacture.

12. We have carefully examined the contractual framework placed on record. Under the Term Sheet dated 06.03.2008, the foreign collaborator granted the appellant non-exclusive rights to establish manufacturing operations in India together with technical support, engineering assistance and product development rights. Under the Royalty Agreement dated 01.04.2010, the appellant was granted rights relating to patents, trademarks, confidential technical know-how and manufacturing technology. Under the Licence Agreement dated 01.04.2012, royalty at the rate of 2% became payable on the net selling price of finished products manufactured and sold by the appellant utilizing CE+T technology.

13. Significantly, none of the aforesaid agreements stipulate that purchase of imported raw materials or components was conditional upon payment of royalty. Equally significant, royalty computation itself was not linked to assessable value or invoice value of imported goods or quantity of imported components or any identifiable link with imports could be traced. The royalty obligation arose only after manufacture of finished products and subsequent commercial sale thereof. This contractual structure clearly demonstrates that royalty was payable for post-import manufacturing rights and commercial exploitation of intellectual property and not as a consideration connected with importation itself.

14. Revenue has argued that imported components constituted essential raw materials for manufacture of finished CE+T branded products and therefore royalty had sufficient nexus with imported goods. In our considered opinion, such reasoning impermissibly expands the scope of Rule 10 of Customs Valuation Rules, 2007. The statutory framework does not contemplate that every payment remotely connected with imported goods automatically becomes includible in assessable value. What the law requires is a direct and proximate relationship between royalty payment and imported goods coupled with proof that such payment constitutes a condition of sale.

15. We also take note of the specific contention advanced by the appellant, as reflected in Para 7.3 of the written submissions that the imported raw materials procured from the related foreign suppliers constituted only a limited portion of the overall raw material procurement undertaken by the appellant for its manufacturing operations in India. In support thereof, the appellant has furnished the year-wise procurement data, reproduced below: -

Financial Year	**Total Raw Materials Purchased (INR)**	**% Imported Raw Materials (Related + Unrelated)**	**% Procured Indigenously**	**Raw Materials Purchased from Related Parties (INR)**	**% Imported from Related Party out of Total Purchases**
2011–2012	3,42,577,763	32%	68%	16,938,315	4.94%
2012–2013	154,816,164	55%	45%	46,927,437	30.31%
2013–2014	391,920,168	73%	27%	21,452,208	5.47%
2014–2015	386,427,476	64%	36%	28,486,345	7.37%

16. The appellant has submitted on the strength of the above data that imports effected from the related foreign supplier constituted only a relatively small proportion of its overall procurement requirements and, except for one financial year, remained below 10% of total raw material purchases on an average. According to the appellant, this factual position itself demonstrates that the royalty payments made under the Term Sheet, Royalty Agreement and Licence Agreement cannot be regarded as payments intrinsically connected with the import transaction, since the appellant was substantially procuring raw materials from

indigenous sources and unrelated suppliers as part of its independent manufacturing operations. We find considerable force in this submission. The above procurement pattern significantly weakens the Department's case that royalty payments were directly relatable to imported goods or that such payments constituted a condition precedent for importation. If the royalty payment was truly linked to imported goods as contended by Revenue, the commercial arrangement would ordinarily reflect a direct dependence on imports from the related supplier. The data placed on record, however, indicates otherwise and reinforces the appellant's contention that the royalty was fundamentally linked to technology transfer, manufacturing rights and post-import commercial exploitation rather than the import transaction itself.

17. We find considerable force in the reliance placed by the appellant on the judicial precedents governing inclusion of royalty in customs valuation, the legal position on the issue being no longer res integra. The Hon'ble Supreme Court in *Ferodo India Pvt Ltd v Commissioner of Customs Mumbai* reported in *2008 (224) E.L.T. 23 (S.C.)* and *Toyota Kirloskar Motor Pvt Ltd v Commissioner of Customs Bangalore* reported in *2007 (213) E.L.T. 4 (S.C.)* have repeatedly held that royalty payments made towards

technical know-how or licence agreements cannot automatically be added to transaction value of imported goods unless Revenue establishes a clear nexus between the royalty payment and the imported goods and further demonstrates that such payment constituted a condition of sale of the imported goods. The ratio emerging consistently from these judgments fully supports the appellant's contention.

18. We also find merit in the appellant's reliance upon the decision of this Tribunal in *M/s. Ajinomoto India Pvt. Ltd. v Commissioner of Customs Chennai II* reported in *2024 (8) TMI 1063 (CESTAT Chennai).* In that case, the Tribunal examined Rule 10(1)(c), Rule 10(1)(e) and the Explanation appended thereto in the context of royalty payable under a Trademark Licence Agreement. The Tribunal categorically held that the Explanation to Rule 10 does not expand the scope of the substantive provision and cannot create an independent basis for inclusion unless the primary statutory requirement of establishing that royalty constituted a condition of sale of imported goods is first satisfied. It was further held that royalty payable for post-import activities, including domestic repacking, use of trademark and commercial exploitation after customs clearance, cannot be added merely because imported goods form part of the

subsequent commercial process. The Tribunal specifically observed that the relevant question is whether import would have taken place if the importer had declined to pay royalty and, in the absence of evidence showing that supply of imported goods was conditional upon such payment, inclusion of royalty in assessable value is impermissible.

19. We also find substantial merit in the reliance placed by the appellant on the another decision of this Tribunal in *Commissioner of Customs Chennai v M/s BBL Daido Pvt Ltd* reported in *2024 (7) TMI 330 (CESTAT Chennai),* wherein this Tribunal examined an almost identical controversy concerning inclusion of royalty payments under Rule 10(1)(c) of the Customs Valuation Rules, 2007 in the context of imports effected from a related foreign supplier under a technology and licence arrangement. In that case also, Revenue sought addition of royalty on the ground that imported raw materials formed part of the finished goods manufactured in India and that royalty computation included the value of imported inputs, thereby establishing nexus between royalty and imported goods. The Tribunal, after examining the Licence and Technical Assistance Agreement as well as the method of computation of royalty, held that mere existence of some direct or indirect nexus between imported raw materials and royalty payment is by itself

insufficient to attract Rule 10(1)(c). It was categorically held that the Department must independently establish the second mandatory statutory requirement, namely that payment of royalty constituted a condition of sale of the imported goods. The Tribunal further emphasized that even where royalty computation includes the value of imported raw materials, such circumstance alone does not justify addition unless the contractual framework specifically establishes that supply or import of goods was conditional upon payment of royalty.

20. Further this Tribunal in BBL Daido Pvt. Ltd. examined the interpretative notes to Rule 10(3) and held that addition under Rule 10 can be sustained only where objective and quantifiable data exists linking royalty exclusively to imported goods. The Tribunal specifically observed that royalty payable for transfer of technology, technical know-how, manufacture of licensed products and use of intellectual property rights remain legally distinct from payments intrinsically connected with importation. Ultimately, the departmental appeal was rejected by holding that even though some nexus with imported raw materials may exist, absence of any contractual stipulation making royalty payment a pre-condition for import or supply of goods is fatal to Revenue’s case. We find that the ratio laid

down in the aforesaid decision squarely supports the appellant's contention in the present appeal. Here also, Revenue has proceeded substantially on the assumption that since imported components were utilized in manufacture of finished CE+T branded products, royalty automatically became includible in assessable value. Such reasoning, in our considered view, directly runs contrary to the legal principle reaffirmed by this Tribunal in BBL Daido Pvt. Ltd., which in turn follows the settled law laid down by the Hon'ble Supreme Court in Ferodo India and Toyota Kirloskar.

21. In view of the contractual framework and settled legal position, we hold that the royalty payments made by the appellant under the contractual agreements do not satisfy the statutory requirements contemplated under Rule 10(1)(c) or Rule 10(1)(e) of the Customs Valuation Rules, 2007 and therefore cannot be added to the assessable value of imported goods.

Issue No. (ii): Whether the impugned orders confirming such inclusion are legally sustainable?

22. Having answered the principal valuation issue in favour of the appellant; we now proceed to examine whether the impugned orders passed by the authorities below sustaining addition of royalty are legally sustainable.

23. We find that in the first round of proceedings, the original adjudicating authority vide Order-in-Original dated 14.03.2014 had examined the relationship between the parties, contractual framework and nature of royalty payments and had specifically concluded that royalty was not liable to be added to assessable value. Revenue thereafter preferred appeal resulting in remand proceedings.

24. However, on examination of the de novo Order-in-Original dated 10.06.2015, we find that no fresh contractual clause, additional documentary evidence or independent material was brought on record establishing that payment of royalty constituted a condition of sale of imported goods. The *de novo* adjudicating authority substantially proceeded on inferential reasoning that since imported components formed part of finished products, royalty necessarily became connected with importation. Such reasoning, in our considered opinion, is contrary to the statutory framework governing Rule 10.

25. The Commissioner (Appeals), while affirming the de novo adjudication, adopted substantially the same reasoning without independently examining whether the mandatory statutory requirements prescribed under Rule 10 stood satisfied. The impugned orders proceed on broad

commercial assumptions rather than strict legal requirements expressly mandated under the Customs Valuation Rules.

26. Customs valuation provisions constitute a statutory code and additions to transaction value are exceptions to acceptance of declared value. Such additions cannot be sustained on generalized assumptions merely because parties are related entities or because imported goods ultimately form part of finished products manufactured domestically. Unless Revenue establishes the precise statutory conditions contemplated under Rule 10, enhancement of assessable value cannot be sustained.

27. We therefore hold that the de novo Order-in-Original No. 38622/2015 dated 10.06.2015 and consequential Order-in-Appeal No. 824/2015 dated 03.09.2015 suffer from fundamental legal infirmity inasmuch as the authorities below have invoked Rule 10(1)(c) read with Rule 10(1)(e) of the Customs Valuation Rules without establishing the mandatory statutory requirements governing inclusion of royalty payments. Consequently, the impugned orders are unsustainable in law.

28. In view of the foregoing discussion, we hold that the royalty payments made by the appellant under the Term Sheet dated 06.03.2008, Royalty Agreement dated 01.04.2010 and Licence Agreement dated 01.04.2012 are not liable to be added to the assessable value of imported goods under Rule 10(1)(c) or Rule 10(1)(e) of the Customs Valuation (Determination of Value of Imported Goods) Rules, 2007. Consequently, the impugned Order-in-Appeal No. 824/2015 dated 03.09.2015 is set aside.

29. The appeal stands allowed with consequential relief, if any, in accordance with law.

(Order pronounced in open court on 22.09.2026)

Sd/-
(AJAYAN T.V.)
MEMBER (JUDICIAL)

Sd/-
(VASA SESHAGIRI RAO)
MEMBER (TECHNICAL)

MK