

Import of goods, revaluation and natural justice

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I am currently working on a case that involves questions of huge significance when it comes to related-party transactions and customs valuation. It is always good to begin with a caveat and I have two. The first is that the import in question pertains to the years 2002-2006, when the Indian custom valuation rules were somewhat different (from what they are now). The second is that I will not comment on the exact merits of the case but provide a broad overview of the legal and practical side of things.

The facts of the case are straightforward. The taxpayer, a company incorporated under the Companies Act, 1956, imported certain raw materials (impure wax) from its US-based parent company between financial years 2002-2003 to 2006-2007. The Commissioner of Customs (Port) referred the case of import to the customs special valuation branch because it was a related-party transaction. After several years - which involved exchange of letters and documentation in support of the invoice value - the transaction value was loaded by a significant percentage and a demand for additional customs duty was made.

First, the law involved. Rule 4(3)(a) of the Customs Valuation Rules, 1988 state: "Where the buyer and seller are related, the transaction value shall be accepted provided that the examination of the circumstances of sale of the imported goods indicate that the relationship did not influence the invoice price."

Para 2 of Interpretative Notes to Rule 4(3) categorically states: "such examination will only be required where there are doubts about the acceptability of the price. Where the proper officer has no doubts about the acceptability of the price, it should be accepted without requesting further information from the importer."

Pertinently, there is a Circular issued by the Central Board of Excise and Customs (Circular No. 11 dated 23.02.2001), which states: "Where...the importer has made an averment that the transactions are between related persons...and there is a, *prima facie justification* for further enquiry, the concerned case of import may be referred to the Special Valuation Branch..."

The taxpayer's contention at the Commissioner Appeals level was that reference to the customs special valuation branch can only be made if there is a *prima facie* justification for further inquiry. On a basic reading of the Circular, there cannot be any quarrel with that contention.

And who decides whether there is a *prima facie* justification or not? The Commissioner of Customs at the Port. The Circular notes that it will be deemed that a *prima facie* case exists for investigation where the importer is not able to provide evidence to the effect that the price has not been influenced by the relationship. So far so good.

The question that arises is the following: can a *prima facie* case exist without critical examination, or any kind of examination for that matter, of the case of import? Would such an examination not involve examination of the imported goods to begin with, i.e. to send the goods for testing purpose to ascertain the quality or composition of the imported goods etc? Should the importer not be given an opportunity to put forth its case while such an examination is ongoing?

It would not be out of place to mention that cases used to prolong in the special valuation branch for years without any decision or final report (this has now been taken care of to a large extent). This is because the Rules and the Circular do not provide for any timelines within which the entire revaluation proceedings must be completed (though the Madras High Court took a different approach to this in a case decided earlier this year, see *Dalmia Cement (Bharat) Limited*).

Interestingly, custom officers at the port tend to routinely refer all cases to the special valuation branch simply on the basis that the transaction was carried out between related parties. Under the then Customs Act read with the 1988 Rules and the Circular specified above, merely because the parties are related should not and cannot be a basis for either making a reference to the special valuation branch for further inquiry or loading of transaction value.

The customs officers must show mutuality of interest and that the relationship *in fact* influenced the price of the invoices. For this, the customs officers have to go back and undertake a "critical" assessment of whether the price was so influenced. This position was settled by the Supreme Court in 2006 (*Prodelin India*).

No wonder many cases of customs revaluation do not pass the scrutiny of courts. There are several reasons for this, but the most important reason is the lack of evidence to support a *prima facie* case of revaluation. After all, how can courts (note that in customs valuation there is a direct appeal from the tribunal to the Supreme Court) uphold revaluation on the basis of extraneous consideration without any proof of contemporaneous exports in higher prices, or absence of flow back of money, or lack of comparables or improper application of comparables (i.e. comparing apples with oranges).

And finally, the burden of proof. There are a catena of decisions in which the Supreme Court has time and again reiterated that the burden to prove that the fact that the relationship between the importer and exporter indeed influenced the price is on the Revenue, not on the taxpayer. In practice, though, the customs officers tend to evade this by asking the taxpayer to provide information and documents in support of the transaction value. Failure by the taxpayer to prove the requisite information is interpreted to mean that the price of the imported goods was indeed not the market price.

As mentioned above, request for documents must be made at the stage of reference to the special valuation branch as well as at the stage of investigation by the special valuation branch. Because (under the old system) a show cause notice was not issued to the taxpayer, there was a tendency to issue an Order without giving the taxpayer an opportunity to respond. Even in cases where a personal hearing was granted, the documents/information supplied by the taxpayer was only cursorily perused.

A 2013 decision handed down by the Bombay High Court (*Forbo Siegling Movement Systems India Pvt Ltd*) reveals how principles of natural justice may be compromised in the process. Referring the case of import to the special valuation branch without informing the importer or loading the transaction value without providing opportunity of hearing severely compromises natural justice and should have no place in a country run by rule of law.