

# S.MURUGAPPAN

ADVOCATE, HIGH COURT

**ASSISTED BY:**

K.NANCY, B.COM., B.L. (HONS.),  
G.GAUTHAM RAM VITTAL, L.L.B.

**CONSULTANTS:**

GST, CUSTOMS, FOREIGN TRADE LAWS,  
FOREIGN EXCHANGE MANAGEMENT ACT.

## OPINION

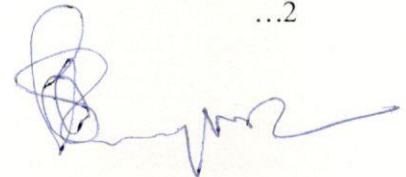
1. **Querist :**

M/s. SKM Egg Products Export (India) Limited,  
20<sup>th</sup> KM, Erode-Karur Road,  
Punjai Kilambadi Village,  
Cholangapalayam,  
Erode District – 638 154.

2. **Facts :**

- 2.1 Querist is an 100% EOU registered under MEPZ, Chennai, manufacturing egg powder and exporting the same to various customers in various countries viz. Europe, Japan, Asian countries at agreed selling price. Similar product was also exported to the querist's own branch in Russia at cost price, being stock transfer from Head office to its foreign branch.
- 2.2 In Russia, none of the local customers are willing to import the products by themselves in order to avoid the cumbersome process. Moreover, it is also not advisable to directly export to the customers in Russia considering the risk factors in receivable management. Hence, querist set up their own branch (not LLC/subsidiary) in Russia to import the products from HO-India, store in a rented warehouse under the title in their name. At this stage, the product is duty paid product. Querist used to sell the imported products locally at Russia based on the orders received from Russian customers. Applicable VAT is being charged in Russia.
- 2.3 The Russian Import duty is @ 15% and it shall be around 80 to 90 USD cents per kg. Querist's Russian Branch operation cost, like Salary, Office Rent, admin, godown rent etc. are around 50 USD cents. But marketing conditions for egg powder at Russia is purely buyer's market and querist is not in a position to sell the products with sufficient profit. Hence, the querist exports to their Branch at cost price to manage the Russian import duty, other costs and able to make a profit of only 10-20 cents per kg. That too, this low margin is possible, only if the querist exports at their cost price, otherwise the additional import duty shall be 30-40 USD cents and their Russian business will end at loss. The querist also properly pays corporate tax on profits earned @ 20% in Russia.

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- 2.4 At this juncture, recently Russian government introduced a law that foreign branches cannot import and sell locally. Hence, querist managed a local company owned by a Russian resident and their branch shall buy locally at Russia from this supplier and sell the same to the same customers at same price. Of course, querist has arrangements with this new supplier at Russia to mark up only 2-3 USD cents per kg, as they only do all the work and only using their name and registration, which they agreed.
- 2.5 If querist converts their branch into Subsidiary/LLP, then profit transfer from Russia to India is again taxable in India, which ends in loss at the end of entire transaction.
- 2.6 Under such circumstances also, querist has to export only at cost price, but not to their foreign branch but to the said outsider party, for their convenience.

**3. Query :**

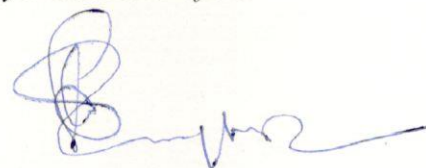
In the above background, querist seeks clarification on the following:

- 3.1 Whether querist's current model of exporting at cost price to their own branch in Russia is acceptable in law.
- 3.2 Whether their continuation of same practice to export under cost price to outside party in Russia (to manage the latest law introduced in Russia) is possible.
- 3.3 In such case, what shall be the documents querist has to maintain to substantiate the taxation authorities in India.
- 3.4 If the opinion is not in their favour, then opine on how to do this export to maintain the profit margin.

**4. Opinion :**

- 4.1 The provisions relating to valuation of export goods that are to be complied with, are contained in Customs Act 1962 and Rules made in terms of the above Act. Section 14 of Customs Act which deals with valuation of import goods as well as export goods reads as follows:

*"SECTION 14. Valuation of goods. — (1) For the purposes of the Customs Tariff Act, 1975 (51 of 1975), or any other law for the time being in force, the value of the imported goods and export goods shall be the transaction value of such goods, that is to say, the price actually paid or payable for the goods when sold for export to India for delivery at the time and place of importation, or as the case may be, for export from India for delivery at the time and place of exportation, where the buyer and seller of the*





*goods are not related and price is the sole consideration for the sale subject to such other conditions as may be specified in the rules made in this behalf :*

**Provided** that such transaction value in the case of imported goods shall include, in addition to the price as aforesaid, any amount paid or payable for costs and services, including commissions and brokerage, engineering, design work, royalties and licence fees, costs of transportation to the place of importation, insurance, loading, unloading and handling charges to the extent and in the manner specified in the rules made in this behalf :

**Provided** further that the rules made in this behalf may provide for,-

- (i) *the circumstances in which the buyer and the seller shall be deemed to be related;*
- (ii) *the manner of determination of value in respect of goods when there is no sale, or the buyer and the seller are related, or price is not the sole consideration for the sale or in any other case;*
- (iii) *the manner of acceptance or rejection of value declared by the importer or exporter, as the case may be, where the proper officer has reason to doubt the truth or accuracy of such value, and determination of value for the purposes of this section :*

**Provided** also that such price shall be calculated with reference to the rate of exchange as in force on the date on which a bill of entry is presented under section 46, or a shipping bill of export, as the case may be, is presented under section 50."

- 4.2 Customs Valuation (Determination of Value of Export Goods) Rules 2007 have been notified by the government of India in terms of the provisions of Customs Act and, in particular, Section 14 mentioned above for the purpose of determining the value of export goods. Copy of the above rules in full is attached to this opinion.
- 4.3 In the present case, it is noticed that the value of the egg powder exported to Russia is less when compared to the value adopted for export of the same egg powder to other countries only for the reason that there is import duty in Russia and as such, if the same price is adopted, it is neither economical nor competitive to sell the goods in the Russian market. At the same time, it is to be noted that the initial exports to Russia were only to the branch of the querist and now, these are routed through an agent and who, in turn, has necessarily to sell the goods to the querist branch only in Russia for further sales. This route has been adopted by the querist for the reasons already explained in the facts.

- 4.4 While Section 14 referred to above and the Valuation Rules mentioned above clearly stipulate that the transaction value will be accepted, it imposes certain conditions for acceptance of such transaction value. In this regard, Rule 3 and Rule 4(1) of Customs Valuation Rules mentioned above will be significant. These rules read as follows:

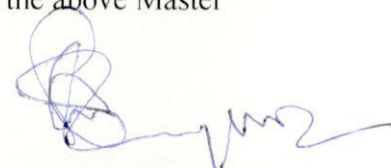
***"RULE 3. Determination of the method of valuation. — (1) Subject to rule 8, the value of export goods shall be the transaction value.***

*(2) The transaction value shall be accepted even where the buyer and seller are related, provided that the relationship has not influenced the price.*

*(3) If the value cannot be determined under the provisions of sub-rule (1) and sub-rule (2), the value shall be determined by proceeding sequentially through rules 4 to 6.*

***RULE 4. Determination of export value by comparison. — (1) The value of the export goods shall be based on the transaction value of goods of like kind and quality exported at or about the same time to other buyers in the same destination country of importation or in its absence another destination country of importation adjusted in accordance with the provisions of sub-rule (2)."***

- 4.5 The adjustments which can be made to the price of the comparable goods are enumerated in Rule 4(2).
- 4.6 In the present case, there is no scope to make adjustments in respect of these factors and therefore, in the normal course, for the same egg powder of same quality exported by the same exporter, export values cannot differ in respect of one country alone when compared to other countries. The important factor to be noted is that price should be the 'sole consideration' and no other factor should influence the price.
- 4.7 As such, there is every scope for the customs authorities to reject the declared value for the purpose of exports and redetermine the value as per the rules mentioned above.
- 4.8 With regard to the provisions of Foreign Exchange Management Act, the Master Direction on Export of Goods and Services bearing No.16/2015-16 dated 01.01.2016, as amended, will be relevant. Para A2 of the above Master Direction reads as follows:



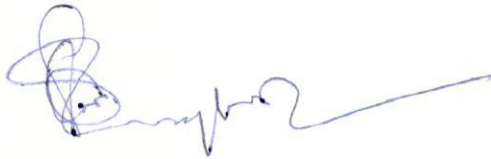


***“A.2 Realization and repatriation of proceeds of export of goods / software / services***

*It is obligatory on the part of the exporter to realize and repatriate the full value of goods / software / services to India within a stipulated period from the date of export, as under:*

*(i) It has been decided in consultation with the Government of India that the period of realization and repatriation of export proceeds shall be nine months from the date of export for all exporters including Units in Special Economic Zones (SEZs), Status Holder Exporters, Export Oriented Units (EOUs), Units in Electronic Hardware Technology Parks (EHTPs), Software Technology Parks (STPs) & Bio-Technology Parks (BTPs) until further notice.”*

- 4.9 Thus, even under FEMA, the exporter is required to realize and repatriate the full value of the goods. The value of the goods for the purpose of this Act will be with reference to the value adopted / determined by customs authorities at the time of export and as reflected in the shipping documents filed with customs.
- 4.10 In the light of the above provisions, we are not in a position to suggest any other way out of this predicament. If one country imposes high import duty, then the market in that country has to develop in a way that the buyers absorb the import duty element to be competitive. If the price is to be reduced for one market, then such a procedure will be in conflict with the provisions of Export Valuation Rules mentioned above.



**S. MURUGAPPAN**

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**Disclaimer:-** The above opinion is provided based on the information and documents made available to us by the querist and further based on the laws and rules prevalent as on date and the understanding of such provisions by the author and is meant for the private use of the person to whom it is provided without assuming any liability for any consequential action taken based on the views expressed here.