

# Bureau of Customs and Border Protection

## *General Notices*

DEPARTMENT OF HOMELAND SECURITY,  
OFFICE OF THE COMMISSIONER OF CUSTOMS.

*Washington, DC, December 28, 2005,*

The following documents of the Bureau of Customs and Border Protection (“CBP”), Office of Regulations and Rulings, have been determined to be of sufficient interest to the public and CBP field offices to merit publication in the CUSTOMS BULLETIN.

Jeremy Baskin for MICHAEL T. SCHMITZ,  
*Assistant Commissioner,  
Office of Regulations and Rulings.*

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### **19 CFR PART 177**

#### **PROPOSED MODIFICATION OF RULING LETTER RELATING TO VALUATION OF MANAGEMENT FEES AND EXPENSES**

**AGENCY:** U. S. Customs and Border Protection, Department of Homeland Security.

**ACTION:** Notice of proposed modification of ruling letter and treatment relating to the valuation of payments made by the buyer of imported merchandise to a related company for management services provided to the buyer.

**SUMMARY:** Pursuant to section 625(c), Tariff Act of 1930 (19 U.S.C. 1625(c)), as amended by section 623 of Title VI (Customs Modernization) of the North American Free Trade Agreement Implementation Act (Pub. L. 103–182, 107 Stat. 2057), this notice advises interested parties that U.S. Customs and Border Protection (“CBP”) intends to modify one ruling letter and any treatment previously accorded by CBP to substantially identical transactions, concerning the inclusion of management fees paid by the buyer of imported mer-

chandise to a related company. CBP invites comments on the correctness of the proposed action.

**DATE:** Comments must be received on or before February 10, 2006.

**ADDRESS:** Written comments are to be addressed to U.S. Customs and Border Protection, Office of Regulations & Rulings, Attention: Trade and Commercial Regulations Branch, 1300 Pennsylvania Avenue N.W., Washington, D.C. 20229. Submitted comments may be inspected at U.S. Customs and Border Protection, 799 9th Street, N.W., Washington, D.C. 20220, during regular business hours. Arrangements to inspect submitted comments should be made in advance by calling Mr. Joseph Clark at (202) 572-8768.

**FOR FURTHER INFORMATION CONTACT:** Gina Grier, Commercial and Trade Facilitation Division (202) 572-8719.

#### **SUPPLEMENTARY INFORMATION:**

##### **Background**

On December 8, 1993, Title VI (Customs Modernization), of the North American Free Trade Agreement Implementation Act (Pub. L. 103-182, 107 Stat. 2057), became effective. Title VI amended many sections of the Tariff Act of 1930, as amended, and related laws. Two new concepts that emerge from the law are **informed compliance** and **shared responsibility**. These concepts are based on the premise that in order to maximize voluntary compliance with CBP laws and regulations, the trade community needs to be clearly and completely informed of its legal obligations. Accordingly, the law imposes a greater obligation on CBP to provide the public with improved information concerning the trade community's rights and responsibilities under the CBP and related laws. In addition, both the trade and CBP share responsibility in carrying out import requirements. For example, under section 484, Tariff Act of 1930, as amended (19 U.S.C. 1484), the importer of record is responsible for using reasonable care to enter, classify and declare value on imported merchandise, and to provide other necessary information to enable CBP to properly assess duties, collect accurate statistics and determine whether any other legal requirement is met.

Pursuant to section 625(c)(1), Tariff Act of 1930 (19 U.S.C. 1625(c)(1)), as amended by section 623 of Title VI, this notice advises interested parties that CBP intends to modify one ruling relating in pertinent part to the valuation of payments made by the buyer of imported merchandise for certain management services provided by a related company. Although in this notice CBP is specifically referring to one ruling, Headquarters Ruling Letter ("HQ") 548316, dated July 16, 2003 (Attachment A), this notice covers any rulings on this issue

that may exist but have not been specifically identified. CBP has undertaken reasonable efforts to search existing databases for rulings in addition to the one identified. No further rulings have been identified. Any party who has received an interpretative ruling or decision (i.e., ruling letter, internal advice memorandum or decision, or protest review decision) on the issues subject to this notice should advise CBP during this notice period.

Similarly, pursuant to section 625(c)(2), Tariff Act of 1930 (19 U.S.C. 1625(c)(2)), as amended by section 623 of Title VI, CBP intends to revoke any treatment previously accorded by CBP to substantially identical transactions. Any person involved in substantially identical transactions should advise CBP during this notice period. An importer's failure to advise CBP of substantially identical transactions or of a specific ruling not identified in this notice, may raise issues of reasonable care on the part of the importer or his agents for importations of merchandise subsequent to the effective date of the final decision on this notice.

In HQ 548316, CBP addressed five issues concerning the determination of transaction value, including the dutiability of certain management fees paid by the buyer to a related company that was not the seller of the imported merchandise. The management fees were to be paid for specific services relating to the importer's sales. CBP held that the payments were not assists and, as such, were not additions to the price actually paid or payable. Although that holding was technically correct, it did not address the more germane issue of whether the payments are included in transaction value as part of the price actually paid or payable for the imported merchandise. HQ 548316 needs to be modified to incorporate a price actually paid or payable analysis of the management fees. Under such an analysis, the modified ruling will reflect that the management fees were not properly included in the price actually paid or payable for the imported merchandise, because they were not paid to, or for the benefit of, the seller and did not relate to the imported merchandise.

In modifying HQ 548316, CBP will also remove any reference to two rulings that are cited in the paragraphs relating to the management fees in the "Law and Analysis" section of HQ 548316. The rulings in question are HQ 543512, dated April 9, 1985, and HQ 542122, dated September 4, 1980 (TAA No. 4). In deference to the court decisions of Generra Sportswear Company v. United States, 905 F.2d 377 (Fed. Cir. 1990) and Chrysler Corporation v. United States, 17 CIT 1049 (1993), CBP no longer accords any weight to HQ 543512, which involved the payment of management fees by the buyer to the seller of imported merchandise. The court cases would demand a different analysis and, possibly, a different result. HQ 542122 examined whether costs for certain management, accounting and legal services constituted dutiable assists under the valuation law. Although it cor-

rectly concluded that the costs were not assists, HQ 542122, too, was issued prior to Generra and did not address the question of whether the payments were included in the price actually paid or payable. Consequently it has limited precedential value here.

As noted above, it is now CBP's position that the payments should not have been included in transaction value as part of the price actually paid or payable, because the payments were not made to the seller and there was no evidence that they benefited the seller in any way. In addition, there was no evidence that the payments were made for the imported merchandise. Pursuant to 19 U.S.C. 1625(c)(1), CBP intends to modify HQ 548316 and any other ruling not specifically identified as set forth in HQ 548547, which is attached as "Attachment B" to this document. Additionally, pursuant to 19 U.S.C. 1625(c)(2), Customs intends to revoke any treatment it previously accorded to substantially identical transactions. Before taking this action, we will give consideration to any written comments timely received.

**DATED:** December 22, 2005

MYLES B. HARMON,  
*Director,*  
*Commercial and Trade Facilitation Division.*

Attachments



[ATTACHMENT A]

DEPARTMENT OF HOMELAND SECURITY.  
BUREAU OF CUSTOMS AND BORDER PROTECTION,  
HQ 548316  
July 16, 2003  
VAL:RR:IT:VA 548316 jsj  
CATEGORY: Valuation

MR. JOHN A. BESSICH  
FOLLIK & BESSICH  
33 Walt Whitman Road Suite 204  
Huntington Station, New York 11746

Re: Assists; Apportionment of Assist; Interest; Finance Service Fees; Management Service Fees; Royalties; Licensing Fees.

DEAR MR. BESSICH:

The purpose of this correspondence is to respond to your request dated April 16, 2003. The correspondence in issue requested, on the behalf of [ABC], a binding valuation ruling concerning the importation of women's garments.

This ruling is being issued subsequent to a review of the following: (1) The submission dated April 16, 2003; (2) A proposed "Design Agreement" be-

tween [ABC] and [XYZ]; (3) An unexecuted "Financing Agreement" between [ABC] and [XYZ]; (4) An unexecuted "Administrative Services Agreement" between [ABC] and [XYZ]; and (4) A proposed "Licensing Agreement" between [ABC] and [XYZ].

Counsel, on the behalf of [ABC], requested confidential treatment for information stated to be commercial or financial information the disclosure of which would prejudice the competitive positions of [ABC] and/or [XYZ]. Customs and Border Protection will, therefore, extend confidential treatment in accordance with the request of counsel for [ABC] dated April 16, 2003. Information determined to be confidential was bracketed in the confidential version and has been redacted and substituted in the public version.

#### FACTS

The relevant entities involved in the proposed transaction are [ABC], a corporation organized under the laws of the State of New York, and [XYZ], a corporation organized under the laws of Spain. Counsel for [ABC] advises the Bureau of Customs and Border Protection (CBP) that [ABC] and [XYZ] are "related parties" as defined in 19 U.S.C. 1401a (g).

It is [ABC]'s intention to market and sell [XXXXX] trademarked women's garments at wholesale in the United States. The garments [ABC] intends to import will be designed by [XYZ], the owner of the [XXXXX] trademark. Although [XYZ] owns the trademark, the garments will be manufactured outside of the United States by manufacturers that are unrelated, as defined in section 1401a (g), to either [ABC] or [XYZ].

[ABC], in the proposed transaction, will order and purchase the garments directly from the foreign manufacturers. The terms between [ABC] and the manufacturers will be "FOB, port of export." [ABC], according to counsel, "will not be required to pay, either directly or indirectly, any royalties, license fees, the proceeds of resale, commissions, or any other costs or charges" as a condition of the sale of the merchandise." [XYZ] will design the garments that [ABC] will have manufactured and will, ultimately, import and sell in the United States.

Counsel for [ABC] advises Customs and Border Protection that [ABC] and [XYZ] will or have already entered into four agreements. The agreements include a design agreement, a financing agreement, an administrative services agreement and a licensing agreement.

#### The Design Agreement

[ABC] and [XYZ] propose entering into a "Design Agreement," a copy of which was provided to CBP. [XYZ], pursuant to the design agreement, will provide [ABC] with design services for the garments that will bear the [XXXXX] trademark. [ABC], CBP is advised, does not have a design staff.

[XYZ] will design, in Spain, the garments that [ABC] will have manufactured outside of the United States and will subsequently import and sell in the United States. [ABC], according to the agreement, will pay [XYZ] directly for all design work. The foreign manufacturers of the garments [ABC] will sell in the United States will not incur any cost for design work and the sales prices of the merchandise from the manufacturers to [ABC] will not include any costs for garment design.

Paragraph 8 of the Design Agreement sets forth the "Design Fee" to be paid by [ABC] to [XYZ]. The design fee is a "per garment design charge" and is determined based on a "three calendar year average" of:

(a) any and all actual out of pocket costs and expenses incurred by [XYZ] directly on account of the design process for each Seasonal Line including but not limited to such costs and expenses incurred in the purchase of sample garments, payments to independent art studios for designs or design services, the aggregate consultation fees paid by [XYZ] to independent contractor designers, the aggregate salaries of [XYZ] dedicated design staff; (b) divided by the total number of garments manufactured by [XYZ], [ABC] and/or any other entity including distributors and licensees using the Designs created for each Seasonal Line during each such calendar year, which amount shall be calculated and adjusted annually throughout the Term.

Counsel for [ABC] advises that the importer will add the “per garment design charge” to the price actually paid or payable at the time of each entry.

#### The Financing Agreement

[ABC] and [XYZ] propose entering into a “Financing Agreement” through which [XYZ] will “fund the operations of [ABC]<sup>TM</sup>s business in the United States.” The agreement, in paragraph 5, obligates [ABC] to pay “[i]nterest on the loans at the prime rate of interest established by Chase Bank, N.A<sup>1</sup>, as computed on the daily debt balances<sup>1</sup>.” The agreement further obligates [ABC] to pay a “service charge for each month<sup>TM</sup>s activities, which shall be \$75 or 1 percent of the aggregate face amount of accounts receivable in which [XYZ] obtains a security interest<sup>1</sup>, whichever is greater.”

[XYZ] is to receive a “continuing security interest” in collateral specifically identified in paragraph 8 of the financing agreement. The foreign manufacturers are not parties to the financing agreement and no payments, either directly or indirectly, will inure to them.

#### The Administrative Services Agreement

[ABC] and [XYZ] have entered into an “Administrative Services Agreement” through which [XYZ] will provide [ABC] with “supervision of and assistance with” its business operations. The business operations encompassed within the administrative services agreement, include but are not limited to: (1) Sales assistance; (2) Promotional assistance; (3) Administrative and bookkeeping assistance; (4) The establishment and maintenance of [ABC]<sup>TM</sup>s books and records; (5) The preparation of financial statements; (6) The rendering of invoices to [ABC] customers; (7) The collection of receivables; (8) The payment of “any and all expenses associated with the business and affairs<sup>1</sup>, including the marketing, sale and promotion of products sold by” [ABC]; (9) The “retention of professionals for all aspects of [ABC]<sup>TM</sup>s business and affairs in the United States;” and (10) “[A]ll other management services required for the efficient operation of [ABC]<sup>TM</sup>s business.”

The administrative services agreement additionally authorizes [XYZ] to incur obligations and borrow money. [XYZ], without the prior approval of [ABC], may incur “any and all obligations or liabilities on the behalf of or for [ABC]<sup>TM</sup>s account” provided these obligations are “in the ordinary course if (sic) business.” The agreement additionally authorizes [XYZ] to “borrow any and all amounts as [ABC] may require from time to time, whether from [XYZ], any institutional lender or factor or otherwise.”

[ABC], in return for the services of [XYZ], agrees to pay a “Management Fee” “equal to five (5%) percent of [ABC]<sup>TM</sup>s gross sales volume anywhere throughout the world.” [ABC] will, additionally, reimburse [XYZ] for the “reasonable expenses” [XYZ] incurs pursuant to the Administrative Services Agreement.

### The Licensing Agreement

The licensing agreement proposed to be entered into between [ABC], as the licensee, and [XYZ], as the licensor, will grant to [ABC] the “non-exclusive” right to use the [XXXXX] trademark in connection with [ABC<sup>TM</sup>s] apparel products and the advertising and promotion of its apparel products. The license will only extend to [ABC<sup>TM</sup>s] operations in the United States and U.S. possessions, territories and military installations.

The agreement provides for the payment of royalties by [ABC] to [XYZ] on a quarterly basis. The royalties, in accordance with paragraph 11 of the Licensing Agreement, will be four percent of the “Net Sales” of the merchandise marketed under the trademark. The term “Net Sales” means “the aggregate of all sales made in the United States in a quarterly period less any and all discounts, returns, allowances, separately stated taxes, freight and insurance.”

### ISSUES

Are the “Design Fees” to be paid by [ABC] to [XYZ] “assists,” as defined in 19 U.S.C. 1401a (h)(1)(A), the value of which must be added to the price actually paid or payable to determine the transaction value of [ABC<sup>TM</sup>s] imported merchandise ?

If the “Design Fees” to be paid by [ABC] to [XYZ] are assists, is the “per garment design charge” proposed by [ABC], as set forth in Paragraph 8 of the Design Agreement, a reasonable method of apportioning the value of the design assist ?

Are the interest and finance service fees payable by [ABC] to [XYZ] pursuant to the “Financing Agreement” additions to the price actually paid or payable in accordance with the transaction value method of appraisement ?

Are the “Management Fees” payable by [ABC] to [XYZ] pursuant to the “Administrative Services Agreement” additions to the price actually paid or payable in accordance with the transaction value method of appraisement ?

Are royalties paid by [ABC] to [XYZ] for the right to use the [XXXXX] trademark on garments manufactured by unrelated, foreign manufacturers and sold by [ABC] in the United States additions to the price actually paid or payable in accordance with the transaction value method of appraisement ?

### LAW AND ANALYSIS

#### Overview

The federal agency responsible for interpreting and applying the United States Code and the regulations of the Bureau of Customs and Border Protection, as they relate to the final appraisement of merchandise, is Customs and Border Protection. Customs and Border Protection, in accordance with its legislative mandate, fixes the final appraisement of imported merchandise in accordance with Section 402 of the Tariff Act of 1930, as amended by the Trade Agreements Act of 1979. □ See 19 U.S.C. 1401a.

The preferred method of appraisement is transaction value. The transaction value of imported merchandise is:

the price actually paid or payable for merchandise when sold for exportation to the United States, plus amounts equal to “(A) the packing costs incurred by the buyer with respect to the imported merchandise; (B) any selling commissions incurred by the buyer with respect to the imported merchandise; the value, apportioned as appropriate, of any assist; any royalty or license fee related to the imported merchandise that

the buyer is required to pay, directly or indirectly, as a condition of the sale of the imported merchandise for exportation to the United States; and (E) the proceeds of any subsequent resale, disposal, or use of the imported merchandise that accrue, directly or indirectly, to the seller. 19 U.S.C. 1401a (b)(1).

The “price actually paid or payable,” as defined in the Trade Agreements Act, is:

the total payment (whether direct or indirect, and exclusive of any costs, charges, or expenses incurred for transportation, insurance, and related services incident to the international shipment of the merchandise from the country of exportation to the place of importation in the United States) made, or to be made, for imported merchandise by the buyer to, or for the benefit of, the seller. 19 U.S.C. 1401a (b)(4)(A).

[ABC] and [XYZ], the parties involved in the proposed Customs transaction, are, according to information presented by counsel, “related” as defined in 19 U.S.C. 1401a (g). Customs and Border Protection, again based on the factual circumstances provided by counsel, does not deem it necessary to review 19 U.S.C. 1401a (b)(2)(B) addressing transaction value between related parties to respond to this ruling request. Although [ABC] is the buyer in the proposed transaction, the seller is not [XYZ] but are, rather, unrelated, foreign manufacturers.

The Design Agreement:

Assists

The transaction value method of appraisement provides that the “transaction value” is the price actually paid or payable “plus amounts equal to - ” (C) the value, apportioned as appropriate, of any assist.” 19 U.S.C. 1401a (b)(1). The term “assist” is defined in 19 U.S.C. 1401a (h). Assist means:

any of the following if supplied directly or indirectly, and free of charge or at a reduced cost, by the buyer of imported merchandise for use in connection with the production or sale for export to the United States of the merchandise:

(i) Materials, components, parts, and similar items incorporated in the imported merchandise.

(ii) Tools, dies, molds, and similar items used in the production of imported merchandise.

(iii) Merchandise consumed in the production of imported merchandise.

(iv) Engineering, development, artwork, design work, and plans and sketches that are undertaken elsewhere than in the United States and are necessary for the production of the imported merchandise. Id.

The “imported merchandise” in the prospective transaction is clothing. The clothing will be designed by [XYZ] in Spain and subsequently manufactured by unrelated foreign manufacturers pursuant to contract(s) entered into between [ABC] and the manufacturers. [ABC], the buyer, will then import the garments into the United States.

The design work is indirectly supplied to the foreign manufacturers by [ABC]. It is supplied free of charge, as [ABC] is responsible for paying [XYZ] for the design work in accordance with their agreement. It will be used in



connection with the production of the merchandise exported to the United States and is necessary for the production of the clothing. It is the determination of this office that the fashion "design work" is an assist, the value of which must be appropriately apportioned to properly determine the transaction value of [ABC]<sup>TM</sup>s entries.

#### Apportionment of Assist

Customs and Border Protection, having determined that the design work is an assist, must now determine whether the method of apportioning the cost of the design work proposed by [ABC] is consistent with the valuation statute and Customs Regulations. CBP regulations, particularly, 19 C.F.R. 152.103 (e)(1), provide in part:

The apportionment of the value of assists to imported merchandise will be made in a reasonable manner appropriate to the circumstances and in accordance with generally accepted accounting principles. The method of apportionment actually accepted by Customs will depend upon the documentation submitted by the importer.

The importer in the instant ruling request submitted a copy of a "Design Agreement" that proposes to apportion the value of the design assist on a per garment basis. It is CBP<sup>TM</sup>s understanding from a review of the agreement, particularly paragraph 8, that the per garment value of the assist is determined by initially establishing the total value of the assist and then dividing the total value of the assist by the total number of garments manufactured using the design in issue. The total value of the assist is to include:

any and all actual out of pocket costs and expenses incurred<sup>1</sup> directly on account of the design process<sup>2</sup>; including but not limited to such costs and expenses incurred in the purchase of sample garments, payments to independent art studios for designs or design services, the aggregate consultation fees paid by [XYZ] to independent contractor designers, the aggregate salaries of [XYZ] dedicated design staff. See Design Agreement, para. 8.

The total number of garments is to include not only the garments manufactured for export to the United States using the relevant design, but is to encompass all garments manufactured by [XYZ], [ABC] or any other entity.□

Subsequent to determining the total value of the assist, [ABC] and [XYZ] will determine the total number of garments manufactured by [ABC], [XYZ] or any other entity. The value of the assist will then be divided by the number of garments produced to establish the "per garment" value of the assist.

It is the decision of this office that the "per garment design charge" apportionment proposed by [ABC] is a "reasonable method appropriate to the circumstances and in accordance with generally accepted accounting principles." [ABC] may apportion the value of the design assist as it proposes on a per garment basis.

It is the understanding of Customs and Border Protection from a review of the agreement and from counsel<sup>TM</sup>s submission that a link exists between the method of apportionment proposed and the merchandise imported. See HQ 545031 (June 30, 1993). Should it become evident in the actual implementation of the proposed method that a portion of the assist<sup>TM</sup>s value would not be subject to duty, the proposed method would then be found to be unreasonable and not in accordance with Customs regulations.

#### The Financing Agreement:

##### Interest and Finance Servicing Fees

Appraising merchandise pursuant to the transaction value method involves determining, among other matters, the “price actually paid or payable.” 19 U.S.C. 1401a (b)(1). Paragraph (b)(4)(a) of section 1401a states that the “price actually paid or payable” means the total payment made or to be made by the buyer to or for the benefit of the seller for imported merchandise, whether the payment is made directly or indirectly, with certain enumerated exclusions.

Counsel suggests in this ruling request that the “price actually paid or payable” should not include the interest payments and finance service charges to be paid by [ABC], as the borrower, to [XYZ], as the lender, pursuant to the proposed financing agreement. Counsel directs the attention of CBP to Treasury Decision (T.D.) 85-111, as published in 50 Fed. Reg. 27886 (1985) and as clarified by Customs in 54 Fed. Reg. 29973 (1989), which sets forth guidelines concerning whether interest payments should be included in the price actually paid or payable. [ABC], through counsel, additionally notes that neither the interest charges nor the service fees will be paid directly or indirectly to the actual sellers, the unrelated, foreign manufactures.

It is the determination of this office that recourse to T.D. 85-111 is not warranted. Since [ABC] and [XYZ] do not have the relationship of buyer and seller, and neither the interest payments or service fees will inure directly or indirectly to the benefit of the unrelated, foreign seller-manufactures, a review of the guidance provided in T.D. 85-111 is not appropriate. The interest payments and finance service charges paid to a lender that is not also the seller should not be included in the price actually paid or payable to determine the transaction value of the relevant entries.

#### The Administrative Services Agreement:

##### Reasonable Expenses Reimbursement and Management Fee Payments

The Administrative Services Agreement presented to Customs and Border Protection, similar to the Financing Agreement, necessitates CBP to determine whether the reimbursement of “reasonable expenses” and the payment of the “Management Fee” set forth in the agreement are sums that must be included in the “price actually paid or payable” pursuant to section 1401a (b)(1) of the Trade Agreements Act. It is the determination of this office, subsequent to a review of the statutory law and prior Customs ruling letters, that the reimbursement of reasonable expenses and the payment of a management fee of five (5) percent of [ABC]’s gross world-wide sales volume as stated in Administrative Services Agreement should not be added to the price actually paid or payable.

The Customs Service in HQ 542122 (Sept. 4, 1980) (TAA No. 4) addressed a similar situation. The issue presented to Customs in TAA No. 4 was whether [m]anagement services, accounting services, legal services and other services related to imported merchandise rendered abroad or in the United States by persons paid by their U.S. employers should be considered assists and added to the price actually paid or payable to determine the transaction value. It was the determination of Customs in TAA No. 4 that the services addressed did not constitute assists and should not be part of

the price actually paid or payable. The reasoning applied in TAA No. 4 is equally applicable to the instant Administrative Services Agreement proposed between [ABC] and [XYZ].

Headquarters Ruling Letter 543512 (April 9, 1998) also addressed a similar transaction and the analysis offered is also applicable. The buyer and seller in HQ 543512 were related parties and the transaction involved the foreign seller-manufacturer, in addition to manufacturing and selling the merchandise in issue, providing “accounting, finance, planning and clerical activities” for the buyer. Customs in HQ 543512 concluded that the fees paid by the buyer to the seller for the “accounting, finance, planning and clerical” services were not dutiable additions to the price actually paid or payable. It was Customs determination that the fees were not dutiable because they were “not tied to the sale for exportation of any specific merchandise.” *Id.* Although the “price actually paid or payable” includes all payments to or for the benefit of the seller, whether direct or indirect, the instant management fees will not be “made, or to be made, for imported merchandise.” 19 U.S.C. 1401a (b)(4)(A).

The Licensing Agreement:

#### Royalty Payments

Section 1401a (b)(1) of the value statute provides for five additions to the “price actually paid or payable” when utilizing the transaction value method of appraising imports for Customs purposes. Royalties and license fees are one of those additions. The price actually paid or payable should be increased to reflect any royalty or license fee related to the imported merchandise that the buyer is required to pay, directly or indirectly, as a condition of the sale of the imported merchandise for exportation to the United States. 19 U.S.C. 1401a (b)(1)(D).

The Statement of Administrative Action (SAA), part of the legislative history of the TAA, reiterating the statute, sets forth that [a]dditions for royalties and license fees will be limited to those that the buyer is required to pay, directly or indirectly, as a condition of the sale of the imported merchandise for exportation to the United States. Statement of Administrative Action, H.R. Rep. No. 153, 96 Cong., 1st Sess., pt. 2, reprinted in, Department of the Treasury, Customs Valuation under the Trade Agreements Act of 1979 (Oct. 1981) at 48–49 (hereinafter SAA).

The SAA continues by noting that the dutiable status of royalty and license fees is determined on a “case-by-case” basis with royalty and license fees paid to third parties for use of copyrights and trademarks in the United States generally considered as a “selling expense of the buyer” and not dutiable. SAA, *id.* The final determination as to dutiability being ultimately dependent on:

- (i) whether the buyer was required to pay them as a condition of sale of the imported merchandise for exportation to the United States; and
- (ii) to whom and under what circumstances they were paid.

SAA, *id.*

The Customs Service, in an effort to further clarify the TAA and the SAA published a General Notice regarding the Dutiability of “Royalty” Payments. See 27 Cust. B. and Dec. 1 (Feb. 10, 1993) (herein after Dutiability of “Royalty” Payments). This issuance is commonly referred to as Hasbro II. Customs, in the General Notice, posed three questions to assist in determining whether royalty or license fees should be dutiable additions to the price ac-

tually paid or payable. The questions are: (1) Was the imported merchandise manufactured under a patent ?; (2) Was the royalty involved in the production or sale of the imported merchandise ?; and (3) Could the importer buy the product without paying the fee ? See generally HQ 546229 (May 31, 1996).

Royalty payments made because imported merchandise was manufactured under a patent or under circumstances in which the royalty was involved in the production or sale of the imported merchandise supports a conclusion that the payments are "related" to the imported merchandise. 19 U.S.C. 1401a (b)(1)(D). The importer's<sup>TM</sup> ability to purchase the merchandise without having to pay a royalty or license fee "goes to the heart of whether a payment is considered to be a condition of sale." Dutiability of "Royalty" Payments, *supra*. Negative answers to questions (1) and (2), and an affirmative response to question (3) supports a determination that royalty payments are not dutiable.

Although CBP has set forth the law regarding whether royalties and license fees paid to third parties should be additions to the price actually paid or payable, this office is not in a position to provide a binding decision concerning the specific transaction proposed by [ABC]. Customs, in a General Notice dated August 8, 1995, advised the trade community that in order for Customs to better address the underlying issues relating to the dutiability of royalty or license fees, especially whether the buyer is required to pay the royalty or license fee as a condition of sale of imported merchandise for exportation to the United States,"a review of the royalty agreement[s] relating to the payment of the royalty or license fees in question and any purchase / supply agreement[s] pertaining to the sale of the imported merchandise for exportation to the United States is necessary. 29 Cust. B. and Dec.10 (Sept. 6, 1995).

This office is, therefore, not able to thoroughly address this issue. Absent an opportunity to review the proposed purchase agreement, CBP is not able to conclusively determine that [ABC], as the buyer, is under no obligation to pay, directly or indirectly, any royalty or license fee to the foreign manufacturers as a condition of the sale.

#### HOLDING

The "Design Fees" to be paid by [ABC] to [XYZ] for designing the garments [ABC] will import into the United States are "assists" which must be appropriately apportioned and added to the price actually paid or payable to establish the transaction value of [ABC's<sup>TM</sup>] entries.

The "per garment design charge" proposed by [ABC], as set forth in Paragraph 8 of the Design Agreement, is a reasonable method of apportioning the value of the design assist.

The interest charges and the finance service fees should not be included in the price actually paid or payable since the lender, [XYZ], is not also the seller of the merchandise proposed to be imported.

The reimbursement of "reasonable expenses" and the payment of the "Management Fee" set forth in the Administrative Services Agreement proposed between [ABC] and [XYZ] are not assists and should not be added to the price actually paid or payable to determine the transaction value of the entries of [ABC].

Customs and Border Protection is unable to determine whether royalty payments proposed to be made by [ABC] to [XYZ] for the right to use the [XXXXX] trademark in the United States in connection with its apparel

products and their advertising and promotion should be an addition to the price actually paid or payable when appraising merchandise for Customs purposes pursuant to the transaction value method of appraisement since Customs and Border Protection was not provided a copy of a proposed purchase or supply agreement.

The regulations of Customs and Border Protection, particularly 19 CFR Â § 177.9(b)(1), provides that "[e]ach ruling letter is issued on the assumption that all of the information furnished in connection with the ruling request and incorporated in the ruling letter, either directly, by reference, or by implication, is accurate and complete in every material respect." The application of a ruling letter by a CBP field office to the transaction to which it is purported to relate is subject to the verification of the facts incorporated in the ruling letter, a comparison of the transaction described therein to the actual transaction, and the satisfaction of any conditions on which the ruling was based.

VIRGINIA L. BROWN,  
*Chief,*  
*Value Branch.*

[ATTACHMENT B]

DEPARTMENT OF HOMELAND SECURITY,  
BUREAU OF CUSTOMS AND BORDER PROTECTION,  
HQ 548547  
VAL:RR:CTF:VS 548547 GG  
CATEGORY: Valuation

MR. JOHN A. BESSICH  
FOLLICK & BESSICH  
33 Walt Whitman Rd. Suite 204  
Huntington Station, New York 11746

Re: Reconsideration of HQ 548316, dated July 16, 2003; valuation of payments for management services rendered to the buyer by a related company that is not the seller

DEAR MR. BESSICH:

This is in reference to Headquarters Ruling Letter (HQ) 548316, dated July 16, 2003, issued to you by this office regarding the valuation of certain imported women's garments. It has come to our attention that our analysis of an issue relating to payments made by the buyer for management services was incorrect. The purpose of this new letter is to modify HQ 548316 by applying the correct analysis. This should have no duty or appraisement consequences – past or future – for your client because under both analyses the payments are found to be not part of the price actually paid or payable. The modification is necessary, however, to prevent any future misunderstanding of our approach to this and similar issues. This letter is essentially a restatement of HQ 548316 except for those places where changes have been made with respect to the discussion of the management fees. As in HQ 548316, confidential treatment is being accorded this reconsideration.

## FACTS

The relevant entities involved in the proposed transaction are ABC, a corporation organized under the laws of the State of New York, and XYZ, a corporation organized under the laws of Spain. Counsel for ABC advises the Bureau of Customs and Border Protection (CBP) that ABC and XYZ are “related parties” as defined in 19 U.S.C. 1401a (g).

It is ABC’s intention to market and sell [XXXXX] trademarked women’s garments at wholesale in the United States. The garments ABC intends to import will be designed by XYZ, the owner of the [XXXXX] trademark. Although XYZ owns the trademark, the garments will be manufactured outside of the United States by manufacturers that are unrelated, as defined in section 1401a (g), to either ABC or XYZ.

ABC, in the proposed transaction, will order and purchase the garments directly from the foreign manufacturers. The terms between ABC and the manufacturers will be “FOB, port of export.” ABC, according to counsel, “will not be required to pay, either directly or indirectly, any royalties, license fees, the proceeds of resale, commissions, or any other costs or charges . . . as a condition of the sale of the merchandise.” XYZ will design the garments that ABC will have manufactured and will, ultimately, import and sell in the United States.

Counsel for ABC advises Customs and Border Protection that ABC and XYZ will or have already entered into four agreements. The agreements include a design agreement, a financing agreement, an administrative services agreement and a licensing agreement.

**The Design Agreement**

ABC and XYZ propose entering into a “Design Agreement,” a copy of which was provided to CBP. XYZ, pursuant to the design agreement, will provide ABC with design services for the garments that will bear the [XXXXX] trademark. ABC, CBP is advised, does not have a design staff.

XYZ will design, in Spain, the garments that ABC will have manufactured outside of the United States and will subsequently import and sell in the United States. ABC, according to the agreement, will pay XYZ directly for all design work. The foreign manufacturers of the garments ABC will sell in the United States will not incur any cost for design work and the sales prices of the merchandise from the manufacturers to ABC will not include any costs for garment design.

Paragraph 8 of the Design Agreement sets forth the “Design Fee” to be paid by ABC to XYZ. The design fee is a “per garment design charge” and is determined based on a “three calendar year average” of:

- (a) any and all actual out of pocket costs and expenses incurred by XYZ directly on account of the design process for each Seasonal Line including but not limited to such costs and expenses incurred in the purchase of sample garments, payments to independent art studios for designs or design services, the aggregate consultation fees paid by XYZ to independent contractor designers, the aggregate salaries of XYZ dedicated design staff;
- (b) divided by the total number of garments manufactured by XYZ, ABC and/or any other entity including distributors and licensees using the Designs created for each Seasonal Line during each such calendar year, which amount shall be calculated and adjusted annually throughout the Term.

Counsel for ABC advises that the importer will add the “per garment design charge” to the price actually paid or payable at the time of each entry.

#### **The Financing Agreement**

ABC and XYZ propose entering into a “Financing Agreement” through which XYZ will “fund the operations of [ABC’s] business in the United States.” The agreement, in paragraph 5, obligates ABC to pay “[i]nterest on the loans at the prime rate of interest established by Chase Bank, N.A. . . . as computed on the daily debt balances. . . .” The agreement further obligates ABC to pay a “service charge for each month’s activities, which shall be \$75 or 1 percent of the aggregate face amount of accounts receivable in which XYZ obtains a security interest . . . whichever is greater.”

XYZ is to receive a “continuing security interest” in collateral specifically identified in paragraph 8 of the financing agreement. The foreign manufacturers are not parties to the financing agreement and no payments, either directly or indirectly, will inure to them.

#### **The Administrative Services Agreement**

ABC and XYZ have entered into an “Administrative Services Agreement” through which XYZ will provide ABC with “supervision of and assistance with” its business operations. The business operations encompassed within the administrative services agreement, include but are not limited to: (1) Sales assistance; (2) Promotional assistance; (3) Administrative and book-keeping assistance; (4) The establishment and maintenance of [ABC’s] books and records; (5) The preparation of financial statements; (6) The rendering of invoices to ABC customers; (7) The collection of receivables; (8) The payment of “any and all expenses associated with the business and affairs . . . including the marketing, sale and promotion of products sold by” ABC; (9) The “retention of professionals for all aspects of [ABC’s] business and affairs in the United States;” and (10) “[A]ll other management services required for the efficient operation of [ABC’s] business.”

The administrative services agreement additionally authorizes XYZ to incur obligations and borrow money. XYZ, without the prior approval of ABC, may incur “any and all obligations or liabilities on the behalf of or for [ABC’s] account” provided these obligations are “in the ordinary course if (sic) business.” The agreement additionally authorizes XYZ to “borrow any and all amounts as ABC may require from time to time, whether from XYZ, any institutional lender or factor or otherwise.”

ABC, in return for the services of XYZ, agrees to pay a “Management Fee” “equal to five (5%) percent of [ABC’s] gross sales volume anywhere throughout the world.” ABC will, additionally, reimburse XYZ for the “reasonable expenses” XYZ incurs pursuant to the Administrative Services Agreement.

#### **The Licensing Agreement**

The licensing agreement proposed to be entered into between ABC, as the licensee, and XYZ, as the licensor, will grant to ABC the “non-exclusive” right to use the [XXXXX] trademark in connection with [ABC’s] apparel products and the advertising and promotion of its apparel products. The license will only extend to [ABC’s] operations in the United States and U.S. possessions, territories and military installations.

The agreement provides for the payment of royalties by ABC to XYZ on a quarterly basis. The royalties, in accordance with paragraph 11 of the Licensing Agreement, will be four percent of the “Net Sales” of the merchandise marketed under the trademark. The term “Net Sales” means “the ag-

gregate of all sales made in the United States in a quarterly period less any and all discounts, returns, allowances, separately stated taxes, freight and insurance.”

#### ISSUES

Are the “Design Fees” to be paid by ABC to XYZ “assists,” as defined in 19 U.S.C. 1401a (h)(1)(A), the value of which must be added to the price actually paid or payable to determine the transaction value of [ABC’s] imported merchandise ?

If the “Design Fees” to be paid by ABC to XYZ are assists, is the “per garment design charge” proposed by ABC, as set forth in Paragraph 8 of the Design Agreement, a reasonable method of apportioning the value of the design assist ?

Are the interest and finance service fees payable by ABC to XYZ pursuant to the “Financing Agreement” additions to the price actually paid or payable in accordance with the transaction value method of appraisement ?

Are the “Management Fees” payable by ABC to XYZ pursuant to the “Administrative Services Agreement” included in the transaction value as part of the price actually paid or payable?

Are royalties paid by ABC to XYZ for the right to use the [XXXXX] trademark on garments manufactured by unrelated, foreign manufacturers and sold by ABC in the United States additions to the price actually paid or payable in accordance with the transaction value method of appraisement ?

#### LAW AND ANALYSIS

##### Overview

The federal agency responsible for interpreting and applying the United States Code and the regulations of the Bureau of Customs and Border Protection, as they relate to the final appraisement of merchandise, is Customs and Border Protection. Customs and Border Protection, in accordance with its legislative mandate, fixes the final appraisement of imported merchandise in accordance with Section 402 of the Tariff Act of 1930, as amended by the Trade Agreements Act of 1979.<sup>1</sup> See 19 U.S.C. 1401a.

The preferred method of appraisement is transaction value. The transaction value of imported merchandise is:

the price actually paid or payable for merchandise when sold for exportation to the United States, plus amounts equal to –

(A) the packing costs incurred by the buyer with respect to the imported merchandise;

(B) any selling commissions incurred by the buyer with respect to the imported merchandise;

(C) the value, apportioned as appropriate, of any assist;

(D) any royalty or license fee related to the imported merchandise that the buyer is required to pay, directly or indirectly, as a condition of the sale of the imported merchandise for exportation to the United States; and

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<sup>1</sup> See generally, *What Every Member of The Trade Community Should Know About: Customs Value*, an Informed Compliance Publication of Customs and Border Protection available on the World Wide Web site of Customs and Border Protection at [www.cbp.gov](http://www.cbp.gov).



(E) the proceeds of any subsequent resale, disposal, or use of the imported merchandise that accrue, directly or indirectly, to the seller. 19 U.S.C. 1401a (b)(1).

The “price actually paid or payable,” as defined in the Trade Agreements Act, is:

the total payment (whether direct or indirect, and exclusive of any costs, charges, or expenses incurred for transportation, insurance, and related services incident to the international shipment of the merchandise from the country of exportation to the place of importation in the United States) made, or to be made, for imported merchandise by the buyer to, or for the benefit of, the seller. 19 U.S.C. 1401a (b)(4)(A).

ABC and XYZ, the parties involved in the proposed Customs transaction, are, according to information presented by counsel, “related” as defined in 19 U.S.C. 1401a (g). Customs and Border Protection, again based on the factual circumstances provided by counsel, does not deem it necessary to review 19 U.S.C. 1401a (b)(2)(B) addressing transaction value between related parties to respond to this ruling request. Although ABC is the buyer in the proposed transaction, the seller is not XYZ but are, rather, unrelated, foreign manufacturers.

**The Design Agreement: Assists**

The transaction value method of appraisement provides that the “transaction value . . . is the price actually paid or payable . . . plus amounts equal to . . . (C) the value, apportioned as appropriate, of any assist.” 19 U.S.C. 1401a (b)(1). The term “assist” is defined in 19 U.S.C. 1401a (h). Assist means:

any of the following if supplied directly or indirectly, and free of charge or at a reduced cost, by the buyer of imported merchandise for use in connection with the production or sale for export to the United States of the merchandise:

(i) Materials, components, parts, and similar items incorporated in the imported merchandise.

(ii) Tools, dies, molds, and similar items used in the production of imported merchandise.

(iii) Merchandise consumed in the production of imported merchandise.

(iv) Engineering, development, artwork, design work, and plans and sketches that are undertaken elsewhere than in the United States and are necessary for the production of the imported merchandise. *Id.*

The “imported merchandise” in the prospective transaction is clothing. The clothing will be designed by XYZ in Spain and subsequently manufactured by unrelated foreign manufacturers pursuant to contract(s) entered into between ABC and the manufacturers. ABC, the buyer, will then import the garments into the United States.

The design work is indirectly supplied to the foreign manufacturers by ABC. It is supplied free of charge, as ABC is responsible for paying XYZ for the design work in accordance with their agreement. It will be used in connection with the production of the merchandise exported to the United States and is necessary for the production of the clothing. It is the determi-

nation of this office that the fashion “design work” is an assist, the value of which must be appropriately apportioned to properly determine the transaction value of [ABC’s] entries.

#### **Apportionment of Assist**

Customs and Border Protection, having determined that the design work is an assist, must now determine whether the method of apportioning the cost of the design work proposed by ABC is consistent with the valuation statute and Customs Regulations. CBP regulations, particularly, 19 C.F.R. 152.103 (e)(1), provide in part:

The apportionment of the value of assists to imported merchandise will be made in a reasonable manner appropriate to the circumstances and in accordance with generally accepted accounting principles. The method of apportionment actually accepted by Customs will depend upon the documentation submitted by the importer.

The importer in the instant ruling request submitted a copy of a “Design Agreement” that proposes to apportion the value of the design assist on a per garment basis. It is CBP’s understanding from a review of the agreement, particularly paragraph 8, that the per garment value of the assist is determined by initially establishing the total value of the assist and then dividing the total value of the assist by the total number of garments manufactured using the design in issue. The total value of the assist is to include:

any and all actual out of pocket costs and expenses incurred . . . directly on account of the design process . . . including but not limited to such costs and expenses incurred in the purchase of sample garments, payments to independent art studios for designs or design services, the aggregate consultation fees paid by XYZ to independent contractor designers, the aggregate salaries of XYZ dedicated design staff. See Design Agreement, para. 8.

The total number of garments is to include not only the garments manufactured for export to the United States using the relevant design, but is to encompass all garments manufactured by XYZ, ABC or any other entity.<sup>2</sup>

Subsequent to determining the total value of the assist, ABC and XYZ will determine the total number of garments manufactured by ABC, XYZ or any other entity. The value of the assist will then be divided by the number of garments produced to establish the “per garment” value of the assist.

It is the decision of this office that the “per garment design charge” apportionment proposed by ABC is a “reasonable method appropriate to the circumstances and in accordance with generally accepted accounting principles.” ABC may apportion the value of the design assist as it proposes on a per garment basis.

It is the understanding of Customs and Border Protection from a review of the agreement and from counsel’s submission that a link exists between the method of apportionment proposed and the merchandise imported. See HQ 545031 (June 30, 1993). Should it become evident in the actual implementa-

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<sup>2</sup>Customs and Border Protection directs the attention of ABC to HQ 544238 (Oct. 24, 1988) and HQ 545500 (Mar. 24, 1995) in which Customs stated that “[i]f the anticipated production is only partially for exportation to the United States, then the method of apportionment will depend upon documentation submitted by the importer.”

tion of the proposed method that a portion of the assist's value would not be subject to duty, the proposed method would then be found to be unreasonable and not in accordance with Customs regulations.

**The Financing Agreement: Interest and Finance Servicing Fees**

Appraising merchandise pursuant to the transaction value method involves determining, among other matters, the "price actually paid or payable." 19 U.S.C. 1401a (b)(1). Paragraph (b)(4)(a) of section 1401a states that the "price actually paid or payable" means the total payment made or to be made by the buyer to or for the benefit of the seller for imported merchandise, whether the payment is made directly or indirectly, with certain enumerated exclusions.

Counsel suggests in this ruling request that the "price actually paid or payable" should not include the interest payments and finance service charges to be paid by ABC, as the borrower, to XYZ, as the lender, pursuant to the proposed financing agreement. Counsel directs the attention of CBP to Treasury Decision (T.D.) 85-111, as published in 50 Fed. Reg. 27886 (1985) and as clarified by Customs in 54 Fed. Reg. 29973 (1989), which sets forth guidelines concerning whether interest payments should be included in the price actually paid or payable. ABC, through counsel, additionally notes that neither the interest charges nor the service fees will be paid directly or indirectly to the actual sellers, the unrelated, foreign manufactures.

It is the determination of this office that recourse to T.D. 85-111 is not warranted. Since ABC and XYZ do not have the relationship of buyer and seller, and neither the interest payments or service fees will inure directly or indirectly to the benefit of the unrelated, foreign seller-manufactures, a review of the guidance provided in T.D. 85-111 is not appropriate. The interest payments and finance service charges paid to a lender that is not also the seller should not be included in the price actually paid or payable to determine the transaction value of the relevant entries.

**The Administrative Services Agreement: Management Fee Payments**

The Administrative Services Agreement presented to Customs and Border Protection, similar to the Financing Agreement, necessitates CBP to determine whether the payment of the "Management Fee" by ABC to XYZ set forth in the agreement are sums that must be included in the transaction value as part of the "price actually paid or payable" pursuant to section 1401a (b)(1) of the Trade Agreements Act. It is the determination of this office that these payments are not so included.

Several court cases have addressed the meaning of the term "price actually paid or payable." In *Generra Sportswear Co. v. United States*, 905 F.2d 377 (Fed. Cir. 1990), the Court of Appeals for the Federal Circuit considered whether quota charges paid to the seller on behalf of the buyer were part of the price actually paid or payable for the imported goods. In reversing the decision of the lower court, the appellate court held that the term "total payment" is all inclusive and that "as long as the quota payment was made to the seller in exchange for merchandise sold for export to the United States, the payment properly may be included in transaction value, even if the payment represents something other than the per se value of the goods." The court also explained that it did not intend that CBP engage in extensive fact

finding to determine whether separate charges, all resulting in payments to the seller in connection with the purchase of imported merchandise, were for the merchandise or something else.

In *Chrysler Corporation v. United States*, 17 CIT 1049 (1993), the Court of International Trade applied the Generra standard and determined that although tooling expenses incurred for the production of the merchandise were part of the price actually paid or payable for the imported merchandise, certain shortfall and special application fees which the buyer paid to the seller were not a component of the price actually paid or payable. With regard to the latter fees, the court found that the evidence established that the fees were independent and unrelated costs assessed because the buyer failed to purchase other products from the seller and were not a component of the price of the imported engines. It has been CBP's position that, based on Generra, there is a presumption that all payments made by a buyer to a seller, or to a party related to the seller, are part of the price actually paid or payable. However, this presumption may be rebutted by evidence that clearly establishes that the payments, like those in *Chrysler*, are completely unrelated to the imported merchandise. See HQ 547175, dated April 21, 2000, and HQ 545663, dated July 14, 1995. In the case at hand, the Generra presumption does not apply because ABC makes the management payments to XYZ, which is neither a seller of the imported merchandise nor a company related to one of the sellers. Accordingly, the payments at issue are part of the price actually paid or payable only if the evidence establishes that they were for the imported merchandise and were for the benefit of the sellers. Based on the terms of the Agreement, the payments are not connected to the purchase of the imported merchandise but are for management services provided by XYZ to ABC in relation to its U.S. sales. There is no other evidence that the payments are made for the imported merchandise or that they benefit the sellers in any way. Accordingly, based on the facts submitted, including the Administrative Services Agreement, the payments are not included in transaction value as part of the price actually paid or payable for the imported merchandise.

We further note that the services provided by XYZ to ABC do not fall within the definition of the term "assist" as defined in 19 U.S.C. § 1401a (h). Therefore, the value of such services is not properly added to the price actually paid or payable as an assist.

#### **The Licensing Agreement: Royalty Payments**

Section 1401a (b)(1) of the value statute provides for five additions to the "price actually paid or payable" when utilizing the transaction value method of appraising imports for Customs purposes. Royalties and license fees are one of those additions. The price actually paid or payable should be increased to reflect

any royalty or license fee related to the imported merchandise that the buyer is required to pay, directly or indirectly, as a condition of the sale of the imported merchandise for exportation to the United States. 19 U.S.C. 1401a (b)(1)(D).

The Statement of Administrative Action (SAA), part of the legislative history of the TAA, reiterating the statute, sets forth that

[a]dditions for royalties and license fees will be limited to those that the buyer is required to pay, directly or indirectly, as a condition of the sale of the imported merchandise for exportation to the United States. *State-*

*ment of Administrative Action*, H.R. Rep. No. 153, 96 Cong., 1<sup>st</sup> Sess., pt. 2, reprinted in, Department of the Treasury, Customs Valuation under the Trade Agreements Act of 1979 (Oct. 1981) at 48–49 (hereinafter *SAA*).

The *SAA* continues by noting that the dutiable status of royalty and license fees is determined on a “case-by-case” basis with royalty and license fees paid to third parties for use of copyrights and trademarks in the United States generally considered as a “selling expense of the buyer” and not dutiable. *SAA, id.* The final determination as to dutiability being ultimately dependent on:

- (i) whether the buyer was required to pay them as a condition of sale of the imported merchandise for exportation to the United States; and
  - (ii) to whom and under what circumstances they were paid.
- SAA, id.*

The Customs Service, in an effort to further clarify the TAA and the *SAA* published a *General Notice* regarding the *Dutiability of “Royalty” Payments*. See 27 Cust. B. and Dec. 1 (Feb. 10, 1993) (herein after *Dutiability of “Royalty” Payments*). This issuance is commonly referred to as *Hasbro II*. Customs, in the *General Notice*, posed three questions to assist in determining whether royalty or license fees should be dutiable additions to the price actually paid or payable. The questions are: (1) Was the imported merchandise manufactured under a patent?; (2) Was the royalty involved in the production or sale of the imported merchandise ?; and (3) Could the importer buy the product without paying the fee? See generally HQ 546229 (May 31, 1996).

Royalty payments made because imported merchandise was manufactured under a patent or under circumstances in which the royalty was involved in the production or sale of the imported merchandise supports a conclusion that the payments are “related” to the imported merchandise. 19 U.S.C. 1401a (b)(1)(D). The importer’s ability to purchase the merchandise without having to pay a royalty or license fee “goes to the heart of whether a payment is considered to be a condition of sale.” *Dutiability of “Royalty” Payments, supra*. Negative answers to questions (1) and (2), and an affirmative response to question (3) supports a determination that royalty payments are not dutiable.

Although CBP has set forth the law regarding whether royalties and license fees paid to third parties should be additions to the price actually paid or payable, this office is not in a position to provide a binding decision concerning the specific transaction proposed by ABC. Customs, in a *General Notice* dated August 8, 1995, advised the trade community that

in order for Customs to better address the underlying issues relating to the dutiability of royalty or license fees, especially whether the buyer is required to pay the royalty or license fee as a condition of sale of imported merchandise for exportation to the United States . . . a review of the royalty agreement[s] relating to the payment of the royalty or license fees in question and any purchase / supply agreement[s] pertaining to the sale of the imported merchandise for exportation to the United States is necessary. 29 Cust. B. and Dec.10 (Sept. 6, 1995).

This office is, therefore, not able to thoroughly address this issue. Absent an opportunity to review the proposed purchase agreement, CBP is not able to

conclusively determine that ABC, as the buyer, is under no obligation to pay, directly or indirectly, any royalty or license fee to the foreign manufacturers as a condition of the sale.

#### HOLDING

The "Design Fees" to be paid by ABC to XYZ for designing the garments ABC will import into the United States are "assists" which must be appropriately apportioned and added to the price actually paid or payable to establish the transaction value of [ABC's] entries.

The "per garment design charge" proposed by ABC, as set forth in Paragraph 8 of the Design Agreement, is a reasonable method of apportioning the value of the design assist.

The interest charges and the finance service fees should not be included in the price actually paid or payable since the lender, XYZ, is not also the seller of the merchandise proposed to be imported.

The payment of the "Management Fee" by ABC to XYZ set forth in the Administrative Services Agreement is not included in transaction value as part of the price actually paid or payable. The payments also are not assists and thus are not additions to the price actually paid or payable. The holding in HQ 548316 is modified accordingly.

Customs and Border Protection is unable to determine whether royalty payments proposed to be made by ABC to XYZ for the right to use the [XXXXX] trademark in the United States in connection with its apparel products and their advertising and promotion should be an addition to the price actually paid or payable when appraising merchandise for Customs purposes pursuant to the transaction value method of appraisal since Customs and Border Protection was not provided a copy of a proposed purchase or supply agreement.

The regulations of Customs and Border Protection, particularly 19 CFR § 177.9(b)(1), provides that "[e]ach ruling letter is issued on the assumption that all of the information furnished in connection with the ruling request and incorporated in the ruling letter, either directly, by reference, or by implication, is accurate and complete in every material respect." The application of a ruling letter by a CBP field office to the transaction to which it is purported to relate is subject to the verification of the facts incorporated in the ruling letter, a comparison of the transaction described therein to the actual transaction, and the satisfaction of any conditions on which the ruling was based.

MYLES B. HARMON,  
*Director,*  
*Commercial and Trade Facilitation Division.*