

# Intercompany Transfer Pricing & Customs Valuation



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# Customs Valuation: 1401a(b)(2) Related Party Rule

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- Customs Valuation Statute 19 USC 1401a
  - 1401a (b)(2)(A) provides that transaction value shall be the appraised value of merchandise only if -
    - \*\*\* (iv) the buyer and seller are not related, or
    - the buyer and seller are related but the transaction value is found to be acceptable
  - Burden is on importer to establish that the relationship does not affect the price



# When are parties related?

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- When are parties related? (19 U.S.C. 1401a(f))
  - (A) Members of the same family.
  - (B) Any officer or director of an organization and such organization.
  - (C) An officer or director of an organization and an officer or director of another organization, if each such individual is also an officer or director in the other organization.
  - (D) Partners.
  - (E) Employer and employee.
  - (F) Any person directly or indirectly owning, controlling, or holding with power to vote, 5 percent or more of the voting stock or shares of any organization and such organization.
  - (G) Two or more persons directly or indirectly controlling, controlled by, or under common control with, any person.



# 1401a(b)(2) Related Party Test

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- The transaction value between a related buyer and seller will be acceptable if:
  - The value of the imported merchandise closely approximates an acceptable “test value”
  - Meets the “circumstances of the sale” test



# 1401a(b)(2) Related Party Test

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- Test Values

- The value of imported merchandise closely approximates
  - Transaction value of identical or similar merchandise in sales to unrelated buyers in the United States; or
  - Deductive or computed value of identical merchandise or similar merchandise from other import transactions.
- Use of “test values”
  - Customs will not accept “test values” as a means of verifying value unless there has been an actual appraisement entry at the test value



# Transaction Value Related Parties

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- The “circumstances of the sale” Test
  - An examination of the “circumstances of the sale” of the imported merchandise indicates that the relationship between the buyer and seller did not influence the price
  - Three methods
    - Price reflects the normal pricing practice for the industry
    - Evidence that the parties negotiated over price
    - Selling price includes all costs plus an amount for profit and general expenses (most common method)



## “Normal Pricing Practices of the Industry”

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- HQ 542261 (Mar. 11, 1981) (TAA No. 19)
  - References to prices published in a trade journal or similar public forum (the posted price) **and**
  - The posted price is used by other buyers and sellers as the basis of contract prices.



# Price Negotiation

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- 543519 dated Sep. 5, 1985, aff'd by 554999 dated Jan. 5, 1989
  - **Documentary evidence must be available** to establish that the parties, although related, bought and sold as if they are not related.
  - The importer **negotiates prices with the** related party seller:
    - rejects the prices if dissatisfied and
    - **may purchase from other suppliers.**
    - The importer's sales divisions determine their U.S. resale prices and make their own management decisions.



# “All Costs Plus Profit” Method

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- 19 C.F.R. 152.103(I)(1)(iii)
  - An importer may demonstrate that the relationship does not influence the price by establishing that:
    - "the price is adequate to ensure recovery of all costs plus
    - a profit that is equivalent to the firm's overall profit realized over a representative period of time in sales of merchandise of the same class or kind . . ."



# Customs Position On Transfer Pricing

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- April 2007, CBP published informed Compliance guide on: TRANSACTION VALUE FOR RELATED PARTY TRANSACTIONS
- Quotes:
  - “The mere fact that the importer has satisfied the requirements of Section 482 IRC, either through an APA or otherwise, does not mean that transaction value is acceptable under 19 U.S.C. §1401a.”
  - “It is still necessary for the importer to analyze whether the related party sale satisfies the circumstances of sale test or the test value method ... before making a value declaration . . .”
  - “An importer that relies solely on an APA or transfer pricing study to conclude that transaction value is acceptable would not be exercising reasonable care.”

- **Customs Brokers**  
- 1/01/2005  
 pdf - 361 KB.
- **Customs Enforcement of Intellectual Property Rights**  
- 03/08/2006  
CBP has determined to remove the informed publication covering IPR from this site until further notice.
- **Customs Value**  
- 07/17/2006  
 pdf - 106 KB.
- **Customs Valuation Encyclopedia (1980 - 2003)**  
- 06/01/2004  
Available for sale through the Superintendent of Documents, U.S. Government Printing Office  
 pdf - 2,604 KB.
- **Decals, Decorative Stickers and Window Clings**  
- 01/24/2007  
 pdf - 96 KB.
- **Decorative Glassware**  
- 03/13/2008  
 pdf - 394 KB.
- **Determining the Acceptability of Transaction Value for Related Party Transactions**  
- 04/26/2007  
 pdf - 135 KB.
- **Diodes, Transistors & Similar Semiconductor Devices**  
- 02/21/2008  
 pdf - 259 KB.
- **Distinguishing Bolts from Screws**  
- 02/21/2008  
 pdf - 210 KB.
- **Drawback**  
- 12/01/2004  
 pdf - 439 KB.



# Acceptability of Transfer Prices Based On “IRS” Transfer Pricing Methodology

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- HQ 546979, August 30, 2000
  - “While the goal of both the TAA and section 482 of the Tax Code is to ensure that the transactions between related parties are at arms length, the method of making that determination is different under each law.”
  - “Customs approach to related party transactions differs from the IRS approach . . . the [IRS] methods review profitability on an aggregate basis, not a product by product basis.”
  - “Customs generally analyzes related party transactions at a more detailed product by product level . . .



# Customs Rulings Addressing Related Party Pricing

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- HQ 546998, dated January 2000-
  - Customs accepts transfer price. Importer provided evidence that profit level of related seller is consistent with normal pricing practice of industry.
- HQ 546979, dated August 2000-- Customs accepts transfer pricing.
  - The transfer pricing methodology had been approved by the IRS through the **Advance Pricing Agreement (APA) Program**;
  - Customs participated in the **APA** pre-filing conference between the Importer and the IRS, and had access to the information provided to the IRS throughout the **APA** process;
  - All of the Importer's imported products were covered by the **APA**.
  - Customs cautioned that any changes in the profit range would need to be reviewed.



# Customs Rulings Addressing Related Party Pricing

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- HQ 548098, May, 2000
  - Customs accepts the transfer price.
  - Submitted detailed information on Seller's pricing to related (U.S.) Party and unrelated (U.K.) Distributor
  - CBP found to be evidence of consistency in pricing.
  - Provided Cost/ Profit breakdown on three selected transactions and showed that profit was higher than seller's overall profit.
  - No IRS TP approach submitted



# Other Related Party Rulings

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- HQ 547672, May 2002 (Volvo Ruling)
  - Customs rejects transfer price as acceptable transaction value.
  - Importer submitted data to suggest that profits of related party seller were in-line with a **range of profits** European contract Mfg. industry.
  - Customs rejects that price was settled in a manner consistent with “normal pricing practices of industry”
  - Information submitted was not specific enough to establish pricing practice of auto industry.
  - Profit level indicator was based on company function and risk, not on products sold, which is required by Customs law.
  - Study looked at aggregate profits and not on individual products.



# Other Related Party Rulings

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- HQ 548095, September 19, 2002
  - Customs rejected transfer price based on Comparable Profits Method.
  - (Comparable range of profits was -0.15% and 10.16%- VSUA was 4%).
  - The Study was not clear that the "comparable companies" referenced were engaged in the sale of High Fashion and/or Designer merchandise.
  - The Study didn't provide detailed information or documentation regarding sellers costs, e.g. accounting records.
  - More importantly however, the distribution agreement indicates that the price between the parties doesn't necessarily have to include a profit.



# Other Related Party Rulings

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- HQ 548233, November 2003
  - Customs accepts transfer price.
  - Importer submits APA agreement accepted by IRS and Japanese Tax authorities to Customs.
  - APA TP method is based on CPM and Modified Resale Price Method that set forth costs and profits of both selling and buying entities.
  - All products were covered by agreement.
  - APA was not conclusive but considered “valuable” information.



# Other Related Party Rulings

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- HQ 548484, July 2004
  - Customs rejects transfer price as acceptable transaction value.
  - Agreement between parties calls for a quarterly pricing adjustment so that “buyer will realize a reasonable operation profit on products purchased from seller.”
  - Profit to be based on range suggested by a CPM analysis of 11 “comparable” companies.
  - Customs was unable to verify that Transfer Pricing Study was sufficient to establish that TP was set in accordance with normal industry pricing practices.
  - Evidence showed that the tested party was the buyer and therefore there was no evidence that the seller received a price that enable recovery of all costs plus a reasonable profit.
  - TP study was not reviewed by IRS and no agreement with conclusions in study.



# Summary: Related Party Pricing

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- Importer should be prepared to provide:
  - Worksheets calculating cost of materials, labor and fixed costs for specific merchandise.
  - Audited financial statements, and information regarding the seller's costs for the subject items and the actual profit.
  - Comparison of actual profit on items under review to profits incurred by company as a whole.



# Valuation: Standard Cost

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- Principles involved in TAA #25 (HLR 542315 dated May 13, 1981)
- In TAA 25 the parties established:
  - The standard cost amount declared on the customs entry represented the **actual amount** paid to the foreign vendor.
  - No payments for variances were subsequently remitted to the related supplier after importation.



# Valuation: Standard Cost—

HQ 544481, May 8, 1991

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- Customs rejected use of standard cost.
- Customs found that adjustments to the standard transfer price were made once a year, as opposed to every three months as in TAA #25.
- The variance between standard and actual costs was an assist to the extent that the standard costs did not reflect the actual costs.
- Customs believed that under these circumstances, unrelated parties would make adjustments to their accounts to remedy the variance between standard and actual costs.
- As noted in TAA #25, these determinations are fact-specific and must be made on a case-by-case basis.



# What Can You Do?

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- Company's "standard cost" or intercompany valuation may not be adequate for Customs valuation purposes.
- Conduct Internal Customs Valuation Study
  - Select one or more of CBP accepted methods of related party pricing
    - **Test values** (TV of Identical or Similar Merchandise/ Deductive or Computed Value)
    - **Circumstances of Sale** (Normal Pricing Practice, Evidence of Negotiation or Cost plus Profit)
  - Select different products or product lines (high volume/ high risk) and test



# What Can You Do?

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- As import manager you may “responsible” for the importation but not the data
- Communicate with Legal, Finance, Tax, Cost Accounting, etc.
  - Share Customs Informed Compliance Publication on “Transfer Pricing For Related Parties”
  - Learn how company derives the invoice values that are reported
  - You should have copies of all intercompany agreements and be advised of proposed changes before they occur